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Royal Commission on Banking and Finance

Central Mortgage & Housing Corporation
Mr. David Mansur.

Hearings held at

OTTAWA

Vol.

49

Date.

17 October 1962



Official Reporters
F.J.Nethercut and R.J.Young
Toronto, Ont.

Netherout & Young
Toronto, Ontario

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ROYAL COMMISSION ON BANKING

AND FINANCE

Hearings held at Ottawa,
Ontario, on Wednesday,
October 17th,1962.

THE COMMISSION

The Honourable Dana Harris Porter
Chief Justice of Ontario
Toronto, Ontario - Chairman

Mr. W. Thomas Brown, M.B.E.
Investment Dealer
Vancouver, British Columbia

Mr. James Douglas Gibson, O.B.E.
Banker
Toronto, Ontario

Mr. Gordon L. Harrold
Agriculturalist
Calgary, Alberta

Mr. Paul H. Leman
Corporation Executive
Montreal, Quebec

Mr. John C. MacKeen
Corporation Executive
Halifax, Nova Scotia

Dr. W.A. Mackintosh
Vice-Chancellor
Queen's University
Kingston, Ontario

Mr. H.A. Hampson - Secretary

Mr. Gilles Mercure - Joint Secretary

Ottawa, Ontario,
Wednesday,
October 17th, 1962.

--- At 9.15 A.M. the hearing resumed.

SUBMISSION OF

CENTRAL MORTGAGE AND HOUSING CORPORATION

APPEARANCES

Mr. Stewart Bates	- President
P. S. Secord	- Vice-President
H.W. Hignett	- Executive Director
R. Adamson	- Chief Economist
A. D. Wilson	- General Counsel

THE CHAIRMAN: I call the meeting to order. The brief this morning is from the Central Mortgage and Housing Corporation. Mr. Bates, President of the Corporation, is present to present the brief and deal with questions. I do not know whether you wish to make a general statement, Mr. Bates, or do you wish us to proceed immediately with the questions? We have all read the brief, I may say, and we are familiar with its contents, so that it is not necessary to go over that again. But if you wish to make any preliminary statement, you are welcome to do so. Otherwise we will proceed with the questions.

MR. BATES: No, sir, I have no statement to

make. I would hope, Mr. Chairman, that in view of the complexity of the subject, from time to time I might rely on my colleagues who are around me to help answer questions.

THE CHAIRMAN: Yes, by all means. Will you now proceed? Would you mind introducing your colleagues, Mr. Bates.

MR. BATES: Yes, Mr. Chairman. The Vice-President of the Corporation is here, Mr. Secord; my Executive Director, Mr. Hignett, on my right; on my left, the Chief Economist, Mr. Adamson; and on his left the legal counsel of the Corporation, Mr. Wilson.

THE CHAIRMAN: Thank you very much.

COMMISSIONER HARROLD: Perhaps we should start with a question on the organization and procedure of the government agency that we have here. You are responsible to the Minister of Public Works, I believe. Is that the department?

MR. BATES: Yes, sir.

COMMISSIONER HARROLD: Could you give us a little idea of the procedure or the direction under which you work. What is the latitude, and so on, that you are allowed from the Minister of Public Works, or just how is it operated?

MR. BATES: Yes, sir. I think, gentlemen, in the case of Central Mortgage and Housing Corporation we have a Minister and a board. In the case of the Bank of Canada, we have a Governor and a board. I am not going to elaborate on these

differences, but they are not subtle; they are real. We have a Minister and a board. If you have had occasion to read the National Housing Act you would see in clause after clause "the Corporation may, with the consent of the Governor in Council, do thus and so", "the Corporation may, with the consent of the Minister, do thus and so". In other words, our operations are tied very, very closely to government. We are not a Crown Corporation, in the sense of being an independent body. We are tied very closely to the Minister and the government. I do not know of any decision I could make without ministerial or governmental consent, except the decision to hire and fire my staff. But everything else relating to housing policy is tied completely to the government, either through the Minister or the Governor in Council.

We really cannot make a loan to a university, for example, or a sewage loan without the consent of the Governor in Council. Our lending policy is determined entirely by the government.

COMMISSIONER HARROLD: You have a board of directors. How are these elected?

MR. BATES: With regard to the board of directors, sir, there are ten members, five of them are public servants and five are drawn from the outside world, architects, and so on; they are drawn from across the country from Vancouver to Halifx. Five are public servants, presumably selected to make sure that the board of directors does not reach decisions which the government could not accept, because there is

th. Department of Finance representative, one from the Deputy Minister of Public Works, two from Central Mortgage, and one from the Privy Council, Mr. Bryce. So that in the board of directors, out of ten members five are senior public servants who should -- they do not have to, but who should know what government policy is on almost any issue. The other five members are from the outside world.

COMMISSIONER HARROLD: They are more or less an advisory board?

MR. BATES: This is so. I think that is a neat way to put it.

COMMISSIONER HARROLD: You have already told us the basis of the selection, and I presume the members you have mentioned, two of them representing CMHC, one the Department of Finance and the other the Deputy Minister of Public Works ---

MR. BATES: And Mr. Bryce, from the Privy Council.

COMMISSIONER HARROLD: That would give you a co-ordination with other departments of government?

MR. BATES: This is so.

COMMISSIONER HARROLD: That is all I have to ask on the organization, I think.

THE CHAIRMAN: Are there any other questions on this aspect of it? I should like to ask two questions about the objectives of housing policy, particularly the government housing policy. Perhaps you could briefly outline what in your view is the objective and the policy laid out by your Corporation.

MR. BATES: The policy, sir, is not laid out by our Corporation; the policy is laid out by the government and we are the instrument through which it is made effective. The policy is set out in the National Housing Act by parliament. I think it could be simply stated, sir, that there are three things in the National Housing Act. One was, and still is, to increase the quantity of housing in Canada; the second was to make a distribution across the country territorially equitable; and the third was to increase the quality of housing in Canada, if possible. I think if we take the whole National Housing Act you could put it down in those three terms. Maybe I am unduly simplifying, sir, but I think this is pretty close to it.

THE CHAIRMAN: At the present time do you feel that those objectives have been reached? Have you sufficiently increased the quantity of housing, for instance?

MR. BATES: Well, in quantitative terms, since the end of the war there has been added to the housing stock one and a half million houses. This is a substantial quantity, since there were only three million at that time, at the end of the war. We have added one and a half million since the end of the war.

THE CHAIRMAN: Is that entirely under the N.H.A., the one and a half million?

MR. BATES: Not entirely, but substantially. 40 per cent is under N.H.A.

THE CHAIRMAN: How much?

MR. BATES: 40 per cent of that increase would

be under N.H.A. I do not think there is any doubt that the quality of housing has improved in the last sixteen years, and since we stand ready to make a loan to anyone anywhere in Canada, I think the territorial distribution can be met and is being met.

Excuse me, sir. Would you re-state your question, and I will give you a different answer. Not a different answer, but a better answer, a more expanded answer. Would you re-state it again, sir.

THE CHAIRMAN: I will try to remember exactly what I said.

MR. BATES: This is my problem exactly.

THE CHAIRMAN: How far have the objectives been achieved as to the increase of quantity of housing? We were dealing with that, I think.

MR. BATES: We are merely dealing with quantity?

THE CHAIRMAN: Yes.

MR. BATES: As I tried to state, sir, the quantity has gone up from three million to four and a half million houses in Canada; not all of it due to us, but a substantial portion of it due to us. And there are no people living in tents, that I know of.

THE CHAIRMAN: That does not indicate very much unless we look at it relatively. There are many houses in existence, houses in various stages of dilapidation , which are still being lived in. Have you any way of assessing the problem as it exists, as it is developing, in the future, the immediate future?

Have you any assessment of the real, what you might call what you consider the real housing needs of the people at the present time, and looking forward perhaps for the next five or ten years?

MR. BATES: Well, We have demographic figures. We know the number of children in high schools. We have a pretty good idea as to the number of these who will start getting married in 1965 onwards, of course. And this would be a very substantial figure, because this will be the post-war baby boom that would move into the housing market from 1965 onwards; and this will be a tremendous figure from 1965 to 1975 in Canada. Of this, there is no question.

You have seen them move through primary school. You have seen them now in high school. I will see them not very long later in the housing market. This is inevitable, and this is a very large figure.

You have asked another question, sir, which is rather difficult for us at Central Mortgage to answer. At least, I think this is the question you are asking. You are saying, how many houses in the metropolitan areas are in need of repair or rehabilitation or destruction. We are not in that business. We know they are there, but we are not in that business. Through the banks we can give home improvement loans, but ---

THE CHAIRMAN: But if you look at the whole housing picture, do not you have to look at the state of existing houses as well as the possible programme of new houses?

COMMISSIONER MACKINTOSH: Have you any

evidence that the proportion of sub-standard houses has been reduced?

MR. BATES: Have we any evidence, sir?

COMMISSIONER MACKINTOSH: Yes.

MR. BATES: What do you mean by"sub-standard houses", sir?

COMMISSIONER MACKINTOSH: You people are always talking about "sub-standard houses". That is where I got the word.

MR. BATES: I am hoist on my own petard here, because Dr. Mackintosh was the director of this Corporation before I came near it.

COMMISSIONER BROWN: You will probably find that he invented that term himself.

MR. BATES: Thank you, sir. Central Mortgage and Housing Corporation, under the National Housing Act, has no instruction to measure anywhere the number of sub-standard houses in Canada. This is essentially a job for the municipalities and the provinces, not C.M.H.C. I think, Dr. Mackintosh, we could give you a pretty good idea, and I think we could dig out a figure from around this table that would be as reasonably close to the truth as we could make it.

I do not think the number of sub-standard houses has decreased very much in the last ten years, because in order to decrease it there are two or three things which must happen. Private enterprise has to go ahead and do clearance, and this it does. Sometimes it is merely a gas station in some street that wipes out three sub-standard houses; sometimes it is a

big development like Ville Marie in Montreal which wipes out sub-standard houses.

COMMISSIONER MACKINTOSH: I hope you are not referring to the St. James' Club.

MR. BATES: Sometimes we in the province, through a partnership, will wipe out sub-standard housing, in the terms of urban re-development; but actually the volume of this clearance is not substantial, no.

It is about 20,000 units a year which are wiped out by one means or another: sometimes it is merely fire -- a gift from God.

COMMISSIONER MACKINTOSH: The only relevance to my question was that it has some bearing on whether your objective of increasing the quality of housing is being attained or whether progress is being made?

MR. BATES: I think you would be quite right in implying that the improvement in quality is essentially in new housing and not in the renovation or rehabilitation of the old. Such improvement as has come has been in new housing rather than redevelopment or rehabilitation.

THE CHAIRMAN: Your system of interest rates, really, amounts to subsidized rates; they don't follow the course of interest rates on the market? They are artificial ones?

MR. BATES: We have no artificial rates, sir.

THE CHAIRMAN: Well, what rates do you impose?

MR. BATES: Under the National Housing Act there is the main rate which is set under Section 4, set by the Governor-in-Council, and this is the maximum rate that lenders can lend under. The maximum rate is 2¼ per cent above the long-term bond rate set by parliament and changed from time to time by the Governor-in-Council; 2¼ per cent above the long term bond rate.

THE CHAIRMAN: Why should it be related to the long-term bond rate?

MR. BATES: You had better ask parliament that question, Mr. Porter.

THE CHAIRMAN: Go ahead; I don't want to interrupt you.

MR. BATES: I wanted to say something else, then we will come back to this, if you don't mind.

We have several rates we lend under in the Corporation in terms of direct lending: we lend to universities, we lend on sewage projects in municipalities; we lend to limited dividend companies; and these rates are defined in the act, again. These rates are set normally at one-eighth above what we borrow at from the government. For instance, if we borrow from the government at five , these rates to limited dividends, universities and others would be 5 1/8. Last month the government raised our borrowing rate from 5 to 5½; so, the rate to these corporations and limited dividends, for old people, low income housing, and so on, went from 5 1/8 to 5 5/8. In other words, we lend according to the act at one-eightth above what we borrow at; that is when we are lending directly.

However, there is that other rate of interest set by the government which determines what the banks, life, trust and other companies can lend at, which today stands at 6½.

THE CHAIRMAN: Your rates, though, are less than the going mortgage rates?

MR. BATES: That is so, on these special things which are defined in the act: limited dividends, universities, municipal sewage projects.

THE CHAIRMAN: What about your ordinary houses?

MR. BATES: 6½; they would go at the same rate as the life and trust companies were lending at. We would lend at the same rate, and that rate is determined by government from time to time. The 6½ rate has been in existence for about a year.

THE CHAIRMAN: The market rate is higher than that, isn't it?

MR. BATES: Well, on what we call conventional mortgages as distinguished from N.H.A., this would be higher than 6½, yes: 7 or 7¼, and in some parts of the country 7½ -- conventional mortgages let out by life, trust and loan companies.

THE CHAIRMAN: What is the purpose of providing for an artificially low rate? Because it is as a result of government interference in this case that the rate on N.H.A. mortgages is lower than the going rate on conventional mortgages?

MR. BATES: Well, this, of course, is one of the purposes of the National Housing Act.

THE CHAIRMAN: Yes, but I want to know what the philosophy is behind it. Why are you selecting this particular phase of activity and applying to it, through funds which are really provided, in effect, by government agencies, a lower rate of interest than the market rate?

MR. BATES: Let me get this completely clear: our rate is the rate on insured mortgages, and

these are not provided by government. Most of the loans at this price are provided by the life, trust and insurance companies by their own choice, because this is an insured mortgage. We come in as a residual lender if there is nobody else there; but this 6½ rate is taken by the life, trust and other companies, and when it was below 6 also by the banks, because it is an insured rate.

THE CHAIRMAN: Insured by whom?

MR. BATES: By the home owner who pays the insurance fee, and he pays it to us. We carry the insurance on this loan, so if anything goes wrong with it they are guaranteed in the event of foreclosure that they will be repaid. So, the bulk of the lending under N.H.A. is not done by the government even today; it is done by the outside companies.

THE CHAIRMAN: And the insurance is a fund that is made up out of premiums?

MR. BATES: The home owner pays a premium of 2 per cent.

THE CHAIRMAN: So that is on a proper insurance basis?

MR. BATES: Yes, sir -- well, we really don't know; we hope so. We don't know how many foreclosures may come if there is a depression.

THE CHAIRMAN: Well, you may have to raise your premiums?

MR. BATES: No, the government is standing behind it.

THE CHAIRMAN: That is what I am trying to get at: how far is the government standing behind these ventures? How far are they, in a sense, government ventures having a certain advantage in that respect over ventures on the regular market? In other words, to what extent are these houses subsidized in one way or another, if at all?

MR. BATES: All right, this is a good question.

THE CHAIRMAN: I am not suggesting it is wrong. I am trying to find out exactly where you stand on it.

MR. BATES: Well, I will try to tell you. The insurance fund was stared in 1954 when the banks were brought into the mortgage business, and this fund was established and was an N.H.A. operation which would cover approved lenders, banks, life and trust companies, and an approximate 2 per cent fee would be paid by the home owner when he bought the house, and in the event of default the fund would reimburse the approved lender. Since 1954 - I can only tell you my experience - defaults have run around the rate of one-half of one per cent of the mortgages covered by this fund. The assets of the fund today are about $95 million, and since 1954 we have paid out $11 million. Defaults are running at about one-half of one percent, and apart from anything like a major depression we cannot see the fund being in trouble to repay life, trust, the bank, or anyone else, on defaults.

So, there is no subsidy in the fund. I think

this is the point you asked me.

THE CHAIRMAN: I wasn't quite sure how that worked, and I very much appreciate having the information.

One of the purposes of the N.H.A. is to improve standards in the construction of houses, isn't it?

MR. BATES: Yes, sir.

THE CHAIRMAN: You lay down certain specifications that must be complied with before money will be advanced on loans, and so on. Could you elaborate on that a little? Just how far do you go in establishing set regulations of that kind?

MR. BATES: Well, at the end of the war the Canadian building industry was not in very good shape. It had had a long period of depression, and during the war itself there wasn't very much building done. At the end of the war, and for a year or two afterwards, there were many new builders coming forward, many of them simply craftsmen, and at that time the Corporation -- and this is before my time -- set up certain standards. Since that time we have changed our position somewhat. The National Research Council worked for some years in setting up a national building code that worked through this on a scientific, technical basis. Actually, today, sir, to answer the question simply, we use the national building code set up by the National Research Council as our basic standards.

THE CHAIRMAN: And those apply to houses of a certain type and size only?

MR. BATES: Anything which we finance or on

which we insure. Everything else is beyond our competence; there is nothing we can do about that.

THE CHAIRMAN: How far do you go in insuring and financing houses? Are your activities limited to houses of a certain size?

MR. BATES: Yes. This is defined in the act. The maximum loan is $14,200 for a three bedroom house; $14,900 for a four bedroom house. Anything above that we have nothing to do with whatever, but up to that level, if they want an N.H.A. loan, either directly from us or insured, the national building code set by the National Research Council must be applied.

THE CHAIRMAN: The mortgage is what percentage of the value?

MR. BATES: It can go up to 95 per cent of the first $12,000; 70 per cent afterwards. The maximum loan is $14,200 on a three bedroom house and $14,900 on a four bedroom house. It is 95 per cent of the first $12,000 loaned.

THE CHAIRMAN: So that the down payment is only 5 per cent?

MR. BATES: Indeed.

THE CHAIRMAN: How do you justify that?

MR. BATES: I don't justify it. This was done by parliament. I had nothing to do with it, sir.

THE CHAIRMAN: Well, I thought perhaps you had some ideas. A man buys a house and he puts up 5 per cent in cash?

MR. BATES: On a $12,000 house.

THE CHAIRMAN: All right, a $12,000 house.

MR. BATES: Yes sir, that is right.

THE CHAIRMAN: And the market for houses of that kind might decline and he wants to sell the house, and he loses his down payment and perhaps more.

MR. BATES: Can you tell me anyone who has done this?

THE CHAIRMAN: I think there has been a rising market ever since you started business, hasn't there? Has that aspect of it ever been considered -- the disadvantages of too small a down payment?

MR. BATES: You will recall, Mr. Chairman, that under the earlier parts of the act, before the amendment in 1960, 10 per cent was required, but it was considered then by the government of that day that it was desirable to widen the demand for housing for various reasons, and that the down payment could be reduced. The number of defaults were infinitesimal in this country. It was felt the down payment could be reduced, and parliament saw fit to reduce it to a down payment of 5 per cent on a $12,000 house. I think, sir, our experience in the last two years has not indicated this particular change has made any difference to defaults.

THE CHAIRMAN: And the interest rate on that loan of 95 per cent would be the same as the interest rate on a loan of lesser amount?

MR. BATES: Yes sir, it would be a 6½ per cent loan whether we loaned directly or whether it was

done by a life or trust company.

THE CHAIRMAN: Well then, the purchaser of that house is getting more than he could ever get out of the regular mortgage market?

MR. BATES: This is right. This is the purpose of the N.H.A. This is what parliament tells us to do.

THE CHAIRMAN: Yes, but it is the government intervention that makes it possible?

MR. BATES: This is so. It is the act that makes this possible.

THE CHAIRMAN: So that the interest rate paid on that loan of 95 per cent of the value of the property is considerably less than could be supplied through the market?

MR. BATES: Yes, but we have no means of forcing the life company or the trust company or the loan company to make a loan at that rate. They are quite free to make conventional loans at 7¼ or 7½.

THE CHAIRMAN: You say they will make loans up to 95 per cent on that basis?

MR. BATES: Yes, because in this particular part of the market they are insured. It is the insurance feature that attracts them. They will do both: any life company will do both; they will make conventional loans at 7¼ and N.H.A. insured loans at 6½. This is up to them; we have no means of affecting their choice. It is entirely a matter of the distribution of their assets; entirely up to them.

THE CHAIRMAN: You provide for the building

of houses in the way you have described, and for maintaining a sufficiently high standard of building in the way that you have described. Does your Corporation enter at all into the field of marketing houses? Is there any policy adopted of any kind which would facilitate the marketing of houses, when a person finds he has to sell and move to another place to live?

MR. BATES: No, sir.

THE CHAIRMAN: So, unless there is a continuously rising market, or a market that is fairly brisk, naturally, a person may have some difficulty in divesting himself of a house in one town if he has to move to another.

MR. BATES: That is right; he may have difficulty in divesting himself of his car or his washing machine. We are not interested in that.

THE CHAIRMAN: We have found a number of people are interested in that.

MR. BATES: Well, I mean under the act; our instructions from parliament.

THE CHAIRMAN: I am trying to get a view of the limits of your policy and the scope of it.

MR. BATES: Yes.

THE CHAIRMAN: So that your concern apparently has to do with the building of houses, that is, the supply of houses of good standards of construction and on the most convenient possible terms of payment.

MR. BATES: Yes, Mr. Porter, I think so. Maybe I should say this, that indirectly we try to do something about this problem you have mentioned in the sense that we try to prevent a surplus of housing arising in any area so that if someone does have to sell he is not selling in a surplus market. We very consciously try to prevent a surplus of N.H.A. housing in any area. This we prevent very consciously and to that extent indirectly we do help someone who is trying to sell a house.

COMMISSIONER BROWN: You prevent or you avoid creating? Isn't it more an avoidance of creating a surplus? How do you positively prevent?

MR. BATES: Well, today, so far as our lending policy goes we will not lend to any person unless he or she cannot get a loan from a bank or a life or a trust company; in other words, we will not lend indiscriminantly and we will only lend to people who cannot get a loan elsewhere. In other words, there is nothing in our financial policy that will create a surplus.

COMMISSIONER BROWN: You used the word

"prevent"; I don't understand that.

MR. BATES: That is what I mean by "prevent". We are not loaning to speculative builders to go out and build houses.

COMMISSIONER BROWN: It is just a question of the emphasis?

MR. BATES: We are preventing that.

COMMISSIONER BROWN: You are avoiding creating that.

MR. BATES: All right.

COMMISSIONER BROWN: Preventing implies that you can stop other people from doing it.

MR. BATES: No I can't, we can't do this.

COMMISSIONER BROWN: That is what I wanted to get clear.

MR. BATES: Builders can still get speculative loans from life and trust companies but they can't get them from C.M.H.C.; we only loan as the loaner of last resort to a home owner. We don't loan to a builder or for rental accommodation, we only loan to a home owner.

There was a period some years ago when we made builders' loans, but this was limited to economic as distinct from housing problems.

COMMISSIONER MACKINTOSH: You don't restrain a life company ---

MR. BATES: No sir.

COMMISSIONER MACKINTOSH: ---from making N.H.A. loans in an area which you perhaps think is a bit over-built?

MR. BATES: No, we wouldn't refuse but we might say something to them.

COMMISSIONER MACKINTOSH: Express surprise?

MR. BATES: Yes.

THE CHAIRMAN: That is known as moral suasion.

MR. BATES: But really, if they wanted to go ahead and do twenty loans we wouldn't say no.

THE CHAIRMAN: You place considerable emphasis on home ownership, do you not?

MR. BATES: The government does, yes.

THE CHAIRMAN: Well, that apparently is one aspect of the philosophy behind your activities, is it not?

MR. BATES: Yes.

THE CHAIRMAN: Home ownership is considered something of value?

MR. BATES: We will insure rental homes.

THE CHAIRMAN: I was going to come to that, I was going to ask you about the rental policy which you have. Perhaps you will report on that now.

MR. BATES: Well, C.M.H.C. itself doesn't lend to normal rental operations unless they are low income, for low income families.

THE CHAIRMAN: That would be subsidized housing?

MR. BATES: It may be subsidized or it may be that it is a limited dividend operation.

THE CHAIRMAN: I understand that.

MR. BATES: Either of those.

THE CHAIRMAN: That requires some subsidy to carry it generally?

MR. BATES: It is a low rate of interest, yes, but as to other rental housing, we are prepared to insure loans made by life and trust companies but we are not prepared to do this completely indiscriminately. For example, last year -- I have forgotten how many houses there were, but I believe it was 8,000 in Toronto and the life and trust companies were prepared to still pour a substantial volume in this year and we said to them, "No, the market in Toronto is becoming saturated, why don't you let off for a while," and actually we cut the number of loans we would insure down to, I think, this year it was 3,000. However, this didn't stop them, they went ahead on a conventional loan basis, which they are quite prepared to do, but we thought that the Toronto market was becoming a bit saturated the same as the Montreal market.

COMMISSIONER GIBSON: On rental housing?

MR. BATES: Yes.

COMMISSIONER GIBSON: On these units you would take a stronger stand in trying to prevent a surplus than you would on regular single housing units?

MR. BATES: Yes.

COMMISSIONER GIBSON: You said earlier that you wouldn't say no?

MR. BATES: Because this thing gets up into great masses; you know what I mean by high rise masses,

and it gets into certain areas and the area gets a bad name and doesn't get let properly and there are 20 per cent and 30 per cent vacancies, and this is merely a caution on our part.

THE CHAIRMAN: Is this rental all apartment type housing?

MR. BATES: Usually, sir.

THE CHAIRMAN: Are there individual houses?

MR. BATES: No, very seldom; row housing and high rise almost entirely. I don't know of any individual housing that is rental.

THE CHAIRMAN: By row housing, they would be independent houses, but ---

MR. BATES: You know, joined together. In the province of Quebec you get duplexes that are rental housing, but it is the only province in Canada that has small houses as rentals. In other places in Canada it is either row housing or high rise.

COMMISSIONER GIBSON: If you only made 2,000 loans this year ---

MR. BATES: It was 3,000 in Toronto.

COMMISSIONER GIBSON: And 8,000 last year, this is more than caution, isn't it?

MR. BATES: Yes, it is more than a caution; it is a real rationing.

COMMISSIONER GIBSON: It is a definite policy?

MR. BATES: But we can't stop it because all that happens is that instead of building N.H.A. houses they are building conventionals.

THE CHAIRMAN: That sort of rental housing, for what income brackets would that be supplied?

MR. BATES: Well, the stuff we are speaking of now would be housing that would rent at $100 to $150.

MR. WILSON: On a two-bedroom apartment, probably in that range.

MR. BATES: And that is for people with incomes of $5,000 and $6,000 a year.

THE CHAIRMAN: Then, when you have to deal with people with incomes of less than that you really get into the subsidized field, don't you?

MR. BATES: Yes.

THE CHAIRMAN: Could you give us some indication as to what extent that field is being looked after?

MR. BATES: Well, in the whole of Canada there are 8,000 subsidized houses -- in the whole of Canada. These are units. In England since the end of the war 70 per cent of the housing has been subsidized and in Sweden 95 per cent is subsidized. Here in Canada since the end of the war we built a million and a half units with 8,000 subsidized.

Now, I don't think this is the fault of the federal government because they took the attitude in every province that it is up to the province and the municipalities to ask them, ask the federal government for assistance in building subsidized housing. The federal government will put up 75 per cent of the capital cost under Section 36 of the National Housing Act, 75 per cent of the capital cost, 75 per cent of the

subsidy. Despite this magnificent offer we have 8,000 units in Canada.

THE CHAIRMAN: Who are you blaming for that, do you think more than 8,000 are necessary?

MR. BATES: I have no comment, sir.

THE CHAIRMAN: But there must be a number of persons who are in the less than $5,000 bracket, this must be pretty great, and it seems to me that there may be a great gap in the programme?

MR. BATES: Yes, you are quite right; more than half the population of Canada is in the figure which you have just mentioned.

COMMISSIONER GIBSON: And how far is this group helped by the fact that you are helping to build these houses for people of the income which you have just mentioned?

MR. BATES: Well, of course ---

COMMISSIONER GIBSON: It assists them?

MR. BATES: This is so.

THE CHAIRMAN: It would be if the increase in houses built is greater than the increase in the population; you see what I mean?

MR. BATES: Yes.

THE CHAIRMAN: If you merely are keeping pace with the population, the net result is that there are no old houses that are opened up for the lower income groups?

MR. BATES: There are very few empty houses in Canada and there is very little rent reduction and very little cutting in price. We haven't built enough

houses to saturate the market, if that is what you mean, no. But, sir, in this programme of subsidized housing most of it so far has been done in that most sophisticated of all provinces, Ontario, and most of it in Toronto, the wealthiest of all Canadian cities. So that what you see today -- it is only a small portion -- but what you do see is that the poor fisherman of Newfoundland is subsidizing or helping to subsidize the few people in Toronto who live in very nice high rise buildings.

COMMISSIONER HARROLD: Do you include the farmers as well as the fishermen?

MR. BATES: I used to be associated with fishermen, so I automatically think of them.

COMMISSIONER MACKINTOSH: Have you worked out the net value of the subsidy to that Newfoundland fisherman?

MR. BATES: Don't pull my leg, Dr. Mackintosh!

I think, Mr. Porter, in answer to your question, the amount of subsidized housing is very small, but it is likely to increase because in almost all the -- I would say in the fourteen metropolitan areas of Canada -- they have all made studies of their need for urban redevelopment and their need for this kind of thing. It is quite likely to increase very substantially the amount of housing and the amount of subsidy, and this will increase very substantially if the Act remains unchanged, but it has moved faster in Ontario because of the provincial government; the

nature of the provincial government and the nature of the municipalities.

THE CHAIRMAN: But it is very slow?

MR. BATES: It is very slow.

THE CHAIRMAN: And it will continue to be very slow as long as it is left to the provinces and the municipalities to take the brunt ---

MR. BATES: They don't take the brunt, they only take 25 per cent.

THE CHAIRMAN: But isn't that the lower 25 per cent?

MR. BATES: They have to negotiate it.

THE CHAIRMAN: They take the equity position?

MR. BATES: No, no.

THE CHAIRMAN: It is all pro rata, is it?

MR. BATES: Yes.

COMMISSIONER LEMAN: I would like to ask some questions about this. The insurance fund, are there ideas preset as to where it should stop; would you contemplate, if you felt the fund became adequate, reducing the premium for future deals?

MR. BATES: I think that is a very good question, and my answer to it is that I don't know. I don't think anyone knows actuarily what the risks on the fund will really be. When the fund gets hit with a situation like Elliot Lake, where we have 700 houses thrown on the fund immediately, this is a tremendous bite right into it and we really don't know. If we had a depression we don't know what would come on the fund, but no home owner has complained

to us yet of paying 2 per cent premium into the fund. They seem quite content to do this. I mention that the fund is $93 million despite the bite of Elliot Lake. Elliot Lake was a big bite and you might get this anywhere; Thompson, Kitimat, any of the one industry towns, and we have a lot of them in Canada, the one industry towns, where if that industry gets into trouble the whole town is in trouble. So, we have in C.M.H.C. continued to advise the government that so long as home owners are not complaining, that we will let the fund go until we gain some more experience. That is the situation.

COMMISSIONER MACKINTOSH: But the presumption is that if the fund continues to grow and that experience more and more indicated that 2 per cent was more than you needed, the presumption is that it would be adjusted?

MR. BATES: Exactly.

COMMISSIONER MACKINTOSH: But it will be a long time before you have the experience?

MR. BATES: We have now only eight years of experience.

COMMISSIONER MACKINTOSH: There is no presumption that you or the government want to make revenue out of this?

MR. BATES: We are not making revenue; we are holding the funds, we are the trustees of the funds for the insured lenders. In C.M.H.C. we are the trustees of a fund for the insured lenders. If it ran out the government would come to our aid as

it does in the Unemployment Insurance, but we don't want to get into that position if we can help it.

COMMISSIONER LEMAN: Would you just for my information tell me a little bit more about how the payment is paid? Is it paid as a one lump sum payment?

MR. BATES: It gets into the mortgage.

COMMISSIONER LEMAN: It is added to the mortgage?

MR. BATES: Yes, it is added to the mortgage.

COMMISSIONER LEMAN: So therefore it is paid for the life of the mortgage?

MR. BATES: No, it is paid to us directly at the time, but it is in the mortgage, it is part of the mortgage, it is an extra $200 or thereabouts. What would it work out to, about $200? I guess on a normal house it would be that, and the $200, if we are doing a direct loan, we make the direct loan and the $200 comes back to us as trustees. If the bank or an insurance company is making the loan, the $200 comes into the mortgage insurance fund as trustee. There is only one thing we can do with it, we can only buy Canadian government bonds.

COMMISSIONER LEMAN: But the home owner, the fellow that buys this house --

MR. BATES: The cost has gone up to him by $200.

COMMISSIONER LEMAN: Has he paid the $200 at the beginning?

MR. BATES: It is in his mortgage, it is in his loan; he has to pay it over the next 25 years.

COMMISSIONER LEMAN: That is what I was asking, he pays it over the 25 years?

MR. BATES: Yes, he pays it over the 25 years.

COMMISSIONER LEMAN: And the lender pays it to you at the beginning?

MR. BATES: That is right, he pays us immediately.

COMMISSIONER BROWN: Your fund is now $93 million?

MR. BATES: Yes.

COMMISSIONER BROWN: Have you a figure on your potential liability at the moment?

MR. BATES: Yes, $4½ billion.

COMMISSIONER BROWN: This is remaining outstanding?

MR. BATES: That is what is outstanding, $4½ billion.

COMMISSIONER GIBSON: And you said that you put the fund entirely into government Canada bonds?

MR. BATES: That is the instruction in the Act.

COMMISSIONER GIBSON: How do you carry out your investment operations? Do you bear in mind the problems of monetary policy and debt management? Do you buy and trade securities, or do you just buy and keep them?

MR. BATES: We do not trade. We have an agent, the Bank of Canada, that purchases for us, and we do not trade.

COMMISSIONER GIBSON: You are not trading in them?

MR. BATES: No, sir, we are not trading in them. We do not have to.

COMMISSIONER GIBSON: Does the Bank of Canada handle that with advice from you, or is it simply handled by them?

MR. BATES: It handles it for us. It gives us advice.

COMMISSIONER GIBSON: I see.

MR. BATES: It gives us advice, which costs us nothing. The advice is reasonable.

COMMISSIONER HARROLD: Mr. Chairman, perhaps I could ask a question here on the same subject. The question of fishermen and farmers is raised to some extent. Do you see any insuperable difficulty in extending C.M.H.C. loans to the rural areas?

MR. BATES: Yes.

COMMISSIONER HARROLD: Is it a technical difficulty?

MR. BATES: No, sir. They are not growing; there is no rural area that is growing.

COMMISSIONER HARROLD: You are not suggesting that there is not a demand for housing in the rural areas?

MR. BATES: No. We are willing to lend to them.

COMMISSIONER HARROLD: On rural housing?

MR. BATES: Yes, initially. There is just no demand, or very little demand.

COMMISSIONER HARROLD: And there is nothing that would preclude you from lending on a farmhouse, that type of house?

MR. BATES: No, nothing. We do. There is just no demand. We cannot create one.

MR. ADAMSON: The farmers have access to other sources.

COMMISSIONER HARROLD: As far as housing is concerned?

MR. ADAMSON: Yes, sir, and a lot of other things.

COMMISSIONER HARROLD: How about the Farm Credit Corporation and its lending activities on a farm; does that not preclude C.M.H.C. from making a loan on the same property?

MR. WILSON: Only home improvement loans. If a loan qualifies as a farm improvement loan under the Farm Improvement Loans Act, then it cannot be made under the Home Improvement Loans Act, which is now the National Housing Act. But in terms of new construction, a new farm building, a farmer would be entitled to apply for a straight N.H.A. loan on a farmhouse and

would come under our present direct lending policy. If he could not get a loan from anybody else, he could get it from C.M.H.C.

COMMISSIONER GIBSON: But what would the mortgage be based on; would it be based on the farm?

MR. WILSON: The whole farm.

COMMISSIONER HARROLD: With regard to the C.M.H.C. qualifications up to $12,000, he could not borrow $12,000; is that right?

MR. WILSON: No; he could not under the provisions of the National Housing Act, either.

MR. BATES: A farmer can borrow. If he wants to build a house, he can borrow from us.

COMMISSIONER HARROLD: But what would be the limits?

MR. BATES: The same as anybody else, $14,200, $14,900. We would have to have the mortgage on the house, not on the farm. We are not interested in the farm.

THE CHAIRMAN: It is only on the house?

COMMISSIONER MACKINTOSH: This is an important point.

MR. BATES: I am sorry, sir; I made a mistake. My advisers tell me that they would insist on having a mortgage on the whole farm.

THE CHAIRMAN: Then if there is already a mortgage on the farm, a person could not get a loan from you?

MR. BATES: He might be able to. Since I have been in the Corporation I have never had a farm

loan come before me.

COMMISSIONER HARROLD: We have had representation from one of the farm organizations that would like to see the same provisions apply as far as farm housing is concerned, under C.M.H.C., or N.H.A., whatever it may be, and there seem to be technical difficulties in the way of lending just on the house rather than on the whole farm. Is that not right?

MR. WILSON: There is, under the N.H.A., a specific provision to deal with loans for farm housing, which is the only provision placed in the Act where an N.H.A. loan can be used in part to re-finance an existing mortgage on a farm. The limits imposed in the Act are considerably less favourable to the farmer than are provided by the Farm Loans Board, and the maximum loans under the N.H.A., and so on, are less than under the Farm Loans Board provisions, with the result that we get no business. This is basically going through the Farm Loans Board, rather than the National Housing Act. Theoretically and in fact -- legislatively -- there are provisions to remove this technicality, but the limitations are technical.

COMMISSIONER HARROLD: In other words, provided a farmer had a mortgage on the farm, he would not be able to borrow even your $12,000 for a house on the farm?

MR. WILSON: No, sir.

COMMISSIONER GIBSON: One of the problems put to us was that when you have hired help on the farm

and you would like to build them decent housing accommodation, they cannot do this under N.H.A.; you cannot just take a piece of the land and put a house on it and put that up as security.

MR. BATES: I am sorry, sir, but this question has just never come to me. I have never had to face it.

COMMISSIONER HARROLD: I think representation has been made to the government, but it has not got as far as you yet?

MR. BATES: Would this be true, Mr. Wilson, that we could not help finance housing for hired help?

MR. WILSON: We could only use the disencumbered portion of the farm as security for the loan. This puts a limit on the amount of loan the farmer can get under the Act.

We have had experience, and we are continuing to have experience of loans which are not identified as farm loans at all. The farmer has a son who marries; he separates and lives on a one, two or five-acre plot alongside the road; he gets an N.H.A. loan on that, but it is not identified in any sense as a farm loan or a loan to a farmer. But there are actually N.H.A. farm loans to farmers or a farmer's son.

COMMISSIONER BROWN: He has to get a piece of land that is not encumbered by a mortgage elsewhere?

MR. WILSON: Yes, sir.

COMMISSIONER BROWN: If that is done, he can get an N.H.A. loan?

MR. WILSON: Yes.

COMMISSIONER BROWN: What would be the limitation? The same as anywhere else?

MR. WILSON: Yes, exactly the same.

THE CHAIRMAN: Would there be any difficulty arising from the construction standards? You have a formula for this. Would you insist upon that and say that it must be appropriate to the needs of the sort of house the farmer might want to build?

MR. BATES: I do not think so, sir. We have what we call minimum houses that were initially designed for fishermen, that are relatively cheap; one big room, with a few little cubicles going off it -- that sort of thing. We are quite prepared to lend on that type of construction. But there is very little of it asked for. I do not know how many we have lent on. But we are quite prepared to lend on what we call the minimum house; in other words, we would not insist on a town house in a rural area.

THE CHAIRMAN: That is what I had in mind. I did not know whether you had special standards.

MR. BATES: No, sir.

THE CHAIRMAN: As to mortgages on existing houses, you do not provide mortgage money on existing houses at all, do you?

MR. BATES: No, sir, the Act does not provide for this.

THE CHAIRMAN: There has been some suggestion that -- well, we will leave that to a little later on. Are there any further question?

COMMISSIONER BROWN: I should like to ask one

or two questions on this matter of objectives, Mr. Bates. You mentioned quantity, equitable distribution, and quality.

MR. BATES: Yes, sir.

COMMISSIONER BROWN: You did not mention, except obliquely as a result of questions, the matter of encouragement of home ownership; and you did not mention the extent to which combating unemployment entered into it, if this is an objective.

On the other hand, in your brief you say in paragraph 1.41: "From this brief andimpressionistic account it will be appreciated that objectives having little to do with housing as such, have, from the beginning, played an important part in the formulation of housing policy". Would you like to comment on this generally?

MR. BATES: Yes, sir. I think that really from the very beginning of the National Housing Act in 1935 -- remember that it was a question of creating an instrument -- the implications of housing on employment have never been very far away from the government's mind. It is clearly an important employment-creating instrument, because it uses almost entirely Canadian materials; in other words, cement, or earth-moving, or windows, roofs. It is an industry that uses almost entirely domestic materials, and it has therefore been never very far away from employment considerations.

It is not like some of those industries which use a lot of imported materials. This is entirely

an employment-creating industry, and because of its nature, a heavy employer of labour. It is an assembly industry; it is all done by hand; there is practically no machine operation in the final assembly. It requires a very large volume of manpower to build a house, in the assembly as well as in the manufacture of materials. I think, in fact -- to my knowledge, at least, since I have been with the Corporation -- that there has only been really one occasion in which the employment feature has overborne the purely housing feature. That was in the year 1957-58. In 1957-58, in that recession time, the government decided that there was enough potential housing demand to push forward a counter-cyclical, if you like, housing programme; and it did so. The demand at the time was such that it took up the housing.

THE CHAIRMAN: Was that the time when you reduced the down-payment?

MR. BATES: No, sir, this came later. In the 1960 decline of business it was felt that the basic housing demand was not such that housing could be used as a counter-cyclical instrument, and it was not so used. In other words, the demand which has been available in 1957 was not there in 1960, and we might upset the building industry by launching forward with 25 loans per builder, or 50 loans per builder and getting into the speculative building business. So actually in 1960 housing was not used at all as a counter-cyclical measure.

I would think, speaking personally, sir, that I do not see the situation, the conditions of 1957-58

being in front of us for a long time, where we could move ahead with a housing programme far in advance of what we thought the demand could pick up. In other words, it is not available as a counter-cyclical instrument, it seems to us.

COMMISSIONER MACKINTOSH: Because the excess demand is not there?

MR. BATES: This is so, sir.

COMMISSIONER GIBSON: You said earlier, though, that to bring about this filtering down process -- I think that is what it is called --

MR. BATES: Yes, sir.

COMMISSIONER GIBSON: -- whereby there is more housing goes to people in the lower incomes at perhaps more reasonable prices, you need to have a bit of a surplus of housing. From this point of view the over-building of housing is a good thing, I suppose?

MR. BATES: You have to be very brave to face this situation. I think this is true, but you have to be very brave to over-build.

COMMISSIONER GIBSON: If you do not over-build, you do not get this filtering down?

MR. BATES: This is so, sir.

COMMISSIONER GIBSON: So this is a pretty serious part of the policy?

MR. BATES: Yes.

MR. ADAMSON: There is a distinction, though, between over-building in terms of what the demographic requirements will show, and over-building a market.

You may be put in a position where you are not over-building a market, and yet you are adding more houses each year than the normal growth of the population would indicate as a purely physical requirement. In other words, you may be contributing to this filtering down process and not exposing yourself to a market hazard. One is a social and the other a purely economic limit.

COMMISSIONER BROWN: One aspect of this on which I would like to get your opinion is this; the extent to which the policy of encouraging home ownership decreases the mobility of labour in times of economic difficulties.

MR. BATES: I do not really know what that means, sir. If ---

COMMISSIONER BROWN: I will put it this way. Is it a correct assumption, to the extent to which labour, or individuals are renting houses rather than owning them, that there is an increased mobility as between areas?

MR. BATES: There is such a fetish for home ownership. I have not met a Minister yet who was not prepared to rise at any moment in the House of Commons and talk in terms of the virtues of home ownership; what it did for you; it was good for your soul; you could change the storm-windows, tend the garden, look after your children. And apparently this is true. It is true in North America in both the United States and Canada. There is a tremendous fetish for home ownership.

I would think the problem you have mentioned would only arise if the area in which the man was was one in which the market for houses was bad, one industry town that was in trouble, which might reduce the mobility of labour. But I do not think we have any evidence of reduced mobility.

MR. ADAMSON: A lot depends, I suppose, on the conditions in the housing market itself. If it is a very tight housing market, as we had immediately after the war, home ownership is an asset and adds to your mobility.

THE CHAIRMAN: The market is a rising market and the value of the house goes up; it is a good thing in those conditions?

MR. BATES: But if you hit an area like Elliot Lake, I am quite sure this has hurt some people there. And the problem of Sudbury.

MR. ADAMSON: There is the basic fact that the cost of moving from one owned unit to another is much greater than moving from one rented unit to another, for the occupant, because the selling costs of real estate are very considerable. The actual moving of the furniture, the actual physical thing, does not differ very much; but the cost of moving to the home-owner, where he has a very substantial real estate fee to pay, is much greater than with a rented unit.

THE CHAIRMAN: In places like Windsor, which is an automobile centre, if there is slackness in the automobile manufacturing industry it would be almost

impossible to dispose of houses quickly and get out and go somewhere else. It would become a drag on the market very quickly.

MR. BATES: We have no experience of this in Windsor. We own a lot of houses and have sold a lot of houses in Windsor.

THE CHAIRMAN: They don't move.

MR. BATES: It has not been a problem.

THE CHAIRMAN: They don't move.

MR. BATES: No. It has not been a problem.

THE CHAIRMAN: On page 8, Section 1.38:

"The Housing Acts of the 1930's therefore and the Act of 1944 reflected a duality of purposes, the stimulation of economic activity, and the improvement of housing conditions. The purposes were complementary, and not contradictory. Until the Korean crises in 1951 the stimulation of housing and general economic policies reinforced one another. In 1949 down-payments under the Housing Act were materially reduced to stimulate demand and to counteract the business recession then being experienced. In 1951, however, with the rise in defence expenditures and the over-all stimulation of aggregate demand thereby entailed, the first major use of housing policy as an anti-inflationary weapon took place and down-payments were increased under the Act in February of 1951."

Could you give any information as to how successful that policy was at that time.

MR. BATES: This was before my time.

MR. ADAMSON: There was a very sharp drop

in starts in 1951, partly as the result of the government's cutting off a one-sixth loan they had introduced fourteen months earlier; partly also as the result of the withdrawal of the private lenders under the Act in face of rising interest rates which shortly after 1950 became rather more mobile than in the earlier post-war period.

MR. BATES: Looking at the figures, sir, the National Housing Act dropped from 43,000 in 1950 to 21,000 in 1951.

THE CHAIRMAN: Is that in your brief?

MR. BATES: No, it is not in the brief. I am looking at our annual report.

THE CHAIRMAN: What is the net result of all that as to whether the policy was effective?

MR. ADAMSON: It would indicate the policy was effective in that period.

THE CHAIRMAN: The starts dropped after the down-payments were increased.

MR. ADAMSON: Yes.

MR. BATES: I mentioned earlier, sir, that in my time the only counter-cyclical period in which housing was used was 1957-1958. We don't see any sort of circumstance available to us to advise the government to do it again.

THE CHAIRMAN: Well, in 1960 when you increased ---

MR. BATES: We widened the market.

THE CHAIRMAN: Yes, that definitely did widen the market.

MR. BATES: Yes, that is right. I don't think you can widen the market very much more when you get up to 95 per cent loans.

COMMISSIONER BROWN: Until these teenagers start getting married.

MR. BATES: But in terms of changing the Act to bring in more people.

THE CHAIRMAN: When you get to 95 per cent, there isn't much further you can go.

MR. BATES: There is not much left -- there is 105, Mr. Chairman.

--- Short Recess.

COMMISSIONER BROWN: Mr. Bates, I wonder if you could describe for us what the general policies are with regard to participation by private lenders in N.H.A. financing. In the last few years a number of private lenders have dropped out of the N.H.A. scheme. You have suggested that with respect to some of these it was because of the interest rate situation. Were there any other reasons that have been adduced to you, or have any steps been taken to try to encourage the private sector to re-enter the market?

MR. BATES: Well, sir, in the 1954 Act the most significant change was the permission then given to the chartered banks to enter the mortgage lending under the insured section, and the chartered banks did enter in a very substantial way for several years. They withdrew from the market pretty largely in 1959 and 1960, and when the rate of interest went to $6\frac{3}{4}$ the banks, being limited to a 6 per cent lending rate

under the Bank Act, withdrew completely. Naturally, if they had remained in the market the whole volume of demand would have fallen on their shoulders. So, they were through, and there was practically no bank lending since 1960, I think. I think this year there have only been two bank loans made so far. So, the 6 per cent limit on the banks, set up by the Bank Act, was obviously a major factor in this situation.

The other lenders, of course, moved in and out of the housing market, the mortgage market, according to general interest rates -- what they can get here and there -- and in the mortgage market they may be either in the N.H.A. sector or in the conventional sector, whichever suits them better.

So, this is a fairly volatile market in this sense, and it is for this reason that C.M.H.C. has been a residual lender standing behind the mortgage market to make loans if no others were available.

For some years the National Housing Act rate of interest remained unchanged, and the other approved lenders and the banks, who were still in the mortgage market, moved out of the N.H.A. sector into the conventional sector which was more profitable. If the N.H.A. rate had moved a little closer to market rates the proportion between N.H.A. and conventionals would no doubt have remained a little more stable than, in fact, it was. The N.H.A. sector has been more liable to up and down movements partly because it was the rigidity that was in the N.H.A. rate. Actually, the only decrease in the number of lenders has really

been in the chartered banks and, in fact, in the last two or three years we, in C.M.H.C., have taken up almost exactly what the chartered banks had been doing from 1954 to 1958 in lending.

COMMISSIONER BROWN: When you did enter and become the residual lender, what was the basis for deciding the areas to which you would confine yourselves? It wasn't based only the inability to get loans elsewhere? You confined it to certain limited borrowers?

MR. BATES: Well, since 1957 we have been in all areas of Canada.

COMMISSIONER BROWN: I am sorry, I used the word "area" not in the geographical sense.

MR. BATES: I am sorry. We have only been a substantial lender since 1957. Before that our direct lending was quite small. We have been a substantial lender since then, and at one part of the time, as I indicated earlier today, we were engaged in trying to extend the winter programme. The one area we entered at that time was twenty-five loans per builder. The next year it was fifteen -- the figures don't really matter -- but we were in builders' loans at one stage, and this had a very strong employment feature behind it, and the demand seemed adequate to take it up. By 1960 the demand did not seem adequate to take it up, and we stood then as a residual lender not on rentals, not to builders, but only to individual home-owners who could not get a loan from any approved lender. We have been in that position since: that is, we will lend to a home-owner anywhere in Canada who can

produce evidence from two lenders that he cannot get a loan from them. We will lend anywhere in the country, but in terms of your "area" we are only in the home ownership loans.

COMMISSIONER BROWN: And at stages you have only been within certain limits, and so forth: why is all this?

MR. BATES: In one period in the anti-inflationary drive -- I think it was 1960 -- the government informed us we could not spend any more than $150 million, and we had to enter a rationing system that year. In other words, we said, "We will not lend even to a home-owner unless he has an income less than $5,000." This was an anti-inflationary measure for one year.

THE CHAIRMAN: When was that?

MR. BATES: I think it was 1960, sir -- yes, 1960.

This year, for example, we will not spend very much more than that, not because of any anti-inflationary drive, not because of any austerity, but simply because the demand is not there. We will not spend very much more than the $150 million which we did in 1960. But, we had to ration loans then to get it down to that figure, and we used an income qualification. That was the only year we ever had to do that.

COMMISSIONER BROWN: When the terms are changed as they have been from time to time -- the number of years...

MR. BATES: Amortization, you mean?

COMMISSIONER BROWN: Yes. ... percentages, and so forth, has this had an effect on the lenders at all? They have obviously been affected by changes in interest rates?

MR. BATES: Yes.

COMMISSIONER BROWN: And by the interest rate relative to other interest rates; but have lenders shown any changes in attitude because of changes in the other terms?

MR. BATES: Well, I think this would be true, yes. Although we can extend the loan to 30 years, the lender may not wish to go beyond 25 in his amortization period, but I would think it is true to say that the lenders have been quite adaptable, shall we say, to changing circumstances.

However, they are conservative; life companies are naturally a conservative group, you don't expect them to change overnight, but they do change.

COMMISSIONER BROWN: This is despite the fact these are insured loans.

MR. BATES: Yes.

MR. ADAMSON: I think the last change in amortization was in 1960; the authorized maximum went from 30 to 35 years, but even the 30 year maximum was the one which the lenders did not have to observe. The borrower didn't have any entitlement, as it were, to that 30 years, and characteristically didn't get it. Nor has he got the 35 years. It is the 25 years which the borrower may have if he wants it. For the loan to be insured, if the borrower wants it he has to getit. But this is not true of the 35 year limit which the lender may not wish to offer.

COMMISSIONER BROWN: Can you tell us what proportion is the maximum or what is the average?

MR. BATES: I think we might in just a moment. It is above 25 but there is always a change taking place.

MR. SECORD: The borrower has an entitlement

to 25 years and that is in the Act as you know, sir, and I might mention that in our direct lending the loan is made for 25 years or for whatever additional period the borrower requires to keep his payments at 27 per cent of his income, so we have a scale from 25 years up to 35 years. These are on direct loans only.

COMMISSIONER BROWN: While you are looking that up, mention has been made of this 27 per cent and this has been increased at various stages, as I understand it, over the history of the Housing Acts; how was this figure arrived at?

MR. BATES: Oh, I think it is more or less customary usage; pulled out of the air!

COMMISSIONER GIBSON: Did it not start at 23, or something?

MR. BATES: Yes.

COMMISSIONER BROWN: And then it was 25 and then it was 27?

MR. BATES: Yes. I don't think it will go much higher.

MR. HIGNETT: To answer your question, in 1962,6 per cent of all N.H.A.loans made by both the lenders and the Corporation have had amortization periods for longer than 25 years.

MR. ADAMSON: The bulk of those are by us.

MR. HIGNETT: Virtually all the loans made by the lenders are at the 25 year minimum.

MR. ADAMSON: They have been adaptable where

they don't have to adapt.

COMMISSIONER BROWN: You mentioned a moment ago that the number of lenders that are active has not changed materially; can you tell us how many there are?

MR. BATES: I think in a moment we can. There are some approved lenders who don't make any loans.

COMMISSIONER BROWN: I want two figures, one, the number of approved lenders, and the other is the number of active approved lenders.

That is all I have on this, Mr. Chairman.

MR. SECORD: There are 65 lenders who have made loans, and this year there have been 12 lenders -- 12 of the 65 -- who have not made loans this year.

COMMISSIONER BROWN: Thank you very much.

COMMISSIONER LEMAN: Mr. Bates, I would like to go back for one moment to a point you made about the possibilities in the housing field in relation to counter-cyclical action by the government, and I gather that you tell us that as of now and for the foreseeable future there probably wouldn't be a sufficient elasticity of demand for housing to use this as a weapon for activating the economy much. Now, how about in a different sort of circumstances, would it run too much against the objectives of the N.H.A. Act to use it as a restraint instrument in times of ---

MR. BATES: This wasn't done in 1960 when the government instructed us to cut back our lending very substantially and when we had to ration our loans

according to income. This was an anti-inflationary measure. Beyond that I don't think the government could go, and what the approved lenders did was their business, but we had been lending at the rate of $350 million and we were cut back to $150 million -- that is a very substantial cut back -- in 1960.

THE CHAIRMAN: That was in the early part of the year?

MR. BATES: Yes, that is right, Mr. Porter.

THE CHAIRMAN: And it was the end of the year, December I think, when you raised the 90 per cent to 95.

MR. BATES: That is right.

COMMISSIONER LEMAN: That was done by cutting down the number of approved loans. What do you think would be the effect of freeing the rate instead of using it in the way it was used then?

MR. BATES: Freeing the interest rate?

COMMISSIONER LEMAN: Yes.

MR. BATES: You mean, just letting it float, just letting the rate float to wherever it would go?

COMMISSIONER LEMAN: Yes. In other words, getting away from this spread of the N.H.A. rate, et cetera; leaving it to the market.

MR. BATES: Well, it might simply float with the conventional rates.

COMMISSIONER LEMAN: That is one thing which I wanted to ask you about. Have you observed that the conventional mortgage rates have tended to

set themselves into a rather fixed relationship to the N.H.A. rate?

MR. BATES: Not necessarily, although I think it is true that many approved lenders think of some sort of margin as being right and proper, but the relationship between the two rates has varied quite substantially; they haven't kept in parallel with the one per cent margin, or something of this kind. It hasn't been a fixed margin of difference between the two sets.

COMMISSIONER LEMAN: No, it may not be absolutely rigid, but has it tended to act that way in the past?

MR. ADAMSON: I don't think it has. I think from the period from 1957 to 1960 -- roughly that whole three year period in which interest rates generally were rising -- our rate was held at 6 per cent and the conventional rates during parts of that period were well over 7 and up to 7½ at times.

Now, the conventional rates and the N.H.A. rate, particularly in the more recent past, have been quite close together; there has been conventional money available at 7 per cent for much of the past year, and even in special cases I think at 6 3/4 per cent, and this is at a time when our rate has been at 6½ per cent and our rate, you must remember, has the additional feature of a 2 per cent mortgage insurance fee which would represent the equivalent, possibly, of one-quarter per cent on interest rates, so there has not been a tendency, I would say, for the

N.H.A. rate and conventional mortgage interest rates to conform to a fixed pattern.

COMMISSIONER MACKINTOSH: The fact that the lending institutions move in and out of N.H.A. and conventional mortgages is evidence that the rates do not?

MR. BATES: Yes.

COMMISSIONER GIBSON: Plus the lending by the approved lenders, and this chart which appears on page 36 is a very good indication that there is a close relationship between the amount on loan by the approved lenders and the spread between what you might call private mortgage interest rates and the N.H.A. rates, not just conventional mortgage rates.

MR. ADAMSON: Yes, it is not a very mysterious relationship.

COMMISSIONER GIBSON: Mr. Leman asked you what the effect of freeing the rate would be; surely this chart suggests it would tend to stabilize or level out N.H.A. loans to a greater degree than in the past, wouldn't it?

MR. BATES: But at higher levels of interest.

COMMISSIONER GIBSON: But on the average?

MR. BATES: On the average, yes.
In other words, one of the purposes of the N.H.A. would be defeated.

COMMISSIONER GIBSON: But there would still be the insurance feature?

MR. BATES: Yes.

COMMISSIONER GIBSON: Which would have a value?

MR. BATES: Yes.

COMMISSIONER GIBSON: Why would the interest rate be higher on the average; I don't follow that?

MR. BATES: Well, the fact it has always been regulated and that people have been moving in and out indicates that the regulation has from time to time restricted it.

COMMISSIONER GIBSON: Sometimes they don't want the money on those terms?

MR. BATES: Yes.

COMMISSIONER BROWN: For example, the last time you came down from 6 3/4 to 6½, which was in November of 1961, and at the time that you were still at 6 3/4 and before you came down to 6½, were there loans being made at less than 6 3/4 at all?

MR. BATES: Not that we know of.

COMMISSIONER BROWN: They were all at the maximum?

MR. BATES: Yes. There was only one that we know of when the rates were made below the maximum; one brave banker did it.

COMMISSIONER LEMAN: You have explained to us that the business of residential construction must have an influence on economic activity because of the use of Canadian materials, labour, et cetera, and it is nearly 100 per cent Canadian activity, economically speaking. Since you have kept the interest rates, I wouldn't say inflexible, but rather inflexible, could it be that the government felt that as a counter-cyclical

measure it could keep better control with an inflexible rate for the purposes of using housing as a counter-cyclical weapon rather than letting the interest rate flow?

MR. BATES: I don't think that was a consideration, a major consideration, Mr. Leman. I think you have to recognize that when it was first contemplated to raise the National Housing Act rate above 6 per cent that this was a major political decision that had to be made to break through that. The rate had always been much lower and to break through this 6 per cent was a difficult political decision and to go any higher was also a difficult political decision. This was as important as anything else in the considerations at the time, and actually the rate lagged in the market because of political problems, rather than anything else. I suppose the same would happen if we had to contemplate breaking through the 7 per cent ceiling.

COMMISSIONER LEMAN: Mr. Bates, we might come back to the subject which the chairman was opening up earlier in the discussion, which was the question of extending N.H.A. loans to existing houses. You explained to us in paragraphs 4.1 to 4.6 that the financing on the existing houses would not call for all new money because a lot of the properties were already encumbered, but nevertheless in 4.6 you make the statement that perhaps 50 per cent of the flow of funds into residential mortgages is for new houses, and the one which you can look at seems to be 38 per

cent, but because of this refunding back you say it is probably 50 per cent.

Now, what do you believe would be the effect of extending the N.H.A. in terms of existing housing from the point of view of affecting the availability of funds for new housing? Do you agree that it would make a considerable dent in the amount of funds available for new housing?

MR. BATES: Well, I think if the supply of funds were to remain fixed it would make a tremendous dent for some time, a tremendous dent; for three years or five years, I don't know, but a tremendous dent.

COMMISSIONER LEMAN: Would you say that the reason why it would make such a tremendous dent is because the N.H.A. rate is an administered rate and it might not be so if it was a free rate.

MR. BATES: I don't think the rate is so important as the fact that at present under the N.H.A. there is a substantial flow of funds into new housing. Now, if you made a National Housing Act to cover existing housing, part of that flow would inevitably go into existing housing because it is not nearly so fluid a market, especially if you consider giving 95 per cent loans and the same sort of terms as you give on new housing. This would increase tremendously the mobility of movement in the older housing market; many people would sell out and buy automobiles and go to Florida, and I don't know what else, who find it difficult to move today, so the demand on government funds would certainly increase

tremendously, I am sure.

COMMISSIONER LEMAN: It would result in stimulating the durable consumer goods market, perhaps?

MR. BATES: We might just go to Florida, I don't know.

COMMISSIONER LEMAN: One thing which I would like to ask you to make a guess on is this; you have explained to us also that the sources of funds for conventional mortgages are quite different from the sources of funds for new housing because of the N.H.A. Act. In other words, conventional mortgages come from a lot of people who don't even qualify as approved lenders under the N.H.A. Act individually, so is it your thought that opening N.H.A. to existing housing would produce a tremendous shift in the source of funds for the various types of housing?

MR. BATES: I don't know what sort of shift it would mean, but I am quite convinced it would mean a very substantial increase in the demand for funds from the government because ---

COMMISSIONER LEMAN: What I have in mind is this: individuals provide a lot of the conventional mortgage funds?

MR. BATES: Yes.

COMMISSIONER LEMAN: In the market ---

MR. BATES: They might be loaning 60 per cent, but if you are talking of changing the Act to provide 95 per cent, then I don't know whether any individual is actually going to have enough funds to fool around with, so to speak.

COMMISSIONER LEMAN: So the individuals would get out of the market, then?

MR. BATES: I don't know if they would get out, but if they paid in they would be taking 90 and 95 per cent loans instead of 60 per cent loans, and there wouldn't be as much money to go around as there is today, and there would almost inevitably for a period of years be an increased demand on the government to act as a residual lender in that market.

COMMISSIONER LEMAN: Do you visualize that an individual who makes one or two mortgage loans, say, a year would ever become an approved lender under the Act?

MR. BATES: I don't know.

COMMISSIONER LEMAN: Therefore these individuals probably couldn't and wouldn't compete?

MR. BATES: They might not, no.

COMMISSIONER LEMAN: That is what I mean by would you visualize a tremendous shift in really pulling the individuals out of the market, is that your point?

MR. BATES: Well, I think if the N.H.A. applied to the existing housing and borrowers would seek the maximum loans; if they could get them from individuals, all right, but if they couldn't they would expect to get them from us.

COMMISSIONER LEMAN: Some other people have come before the Commission and have suggested that the N.H.A. terms should be extended to existing housing and they made the arguments about it. But they always talked about extending them on exactly the same terms as for new housing, although they admitted that the appraisal system could act as a sort of regulator for this activity. Is there room here for perhaps a middle course? Is it necessary to think of it as extended exactly on the same terms?

MR. BATES: This would be a decision for the government to make, but you are quite right, it could be on quite different terms. Normally most of the people who speak about the extension to existing housing speak in terms of the same sort of legislation as applies to new housing, and inevitably that is where you would get it. You might start off with 80 per cent loans but you would probably get 90 and 95 per cent before too long had passed. I mean, there is the political pressure. The Housing Act is a constant extension of something. It keeps being amended year in and year out. I am quite sure, Mr. Leman, if it started off with an 80 per cent loan it would soon get up to 85 per cent and eventually it would get up to the other level.

COMMISSIONER LEMAN: You see what I am driving at. What I am wondering about is whether the positions taken are so definite that people keep saying if they are extended they should be extended on exactly the same terms, and that may be the reason why the positions

are so firm, you see, on either side.

COMMISSIONER MACKINTOSH: If I could interject here, is it not true that it would have to be varied? You go along and say, "On any new house conforming to N.R.C. standards we will approve a loan of 25 years at least." You cannot do that with existing housing.

MR. BATES: No, this would reflect itself in our appraisals and our lending values on old houses. This is what would happen.

COMMISSIONER MACKINTOSH: It would have to reflect itself also on the terms of lending?

MR. BATES: Yes.

THE CHAIRMAN: Have you any knowledge of any great need for extending any loans to existing housing? Are you familiar enough with the housing market to be able to give us any idea as to how urgent the problem might be?

MR. BATES: Well, as an organization, sir, we have to keep ourselves in preparedness in case we have to launch into that at some date, and therefore we try to keep a watch in every major city on what the market is in used housing, its nature, and so on. We are well aware of the fact that the National Housing Act, by confining itself to new housing, twists the market, if you like, in a way that induces young people with $500 to go into a new house rather than an old house. We are well aware of this. We are well aware of the fact that the volume of mortgage lending by the conventional lenders in the used housing market creates problems in secondary mortgages. We keep our

eye on this. There is nothing we can do about it but we keep our eye on it. We know that if we were in the used housing market the problem of secondary mortgages could be much diminished for many people, but beyond this we do not go except we just keep watching.

THE CHAIRMAN: Is there any indication that there is a lack of a market, that there are areas in the country where it is almost impossible to sell a house, or is the market fairly active? There are people who want to sell houses and there are people prepared to buy them and they will agree on a price.

MR. BATES: There is a very active market.

THE CHAIRMAN: There is?

MR. BATES: Of this there is no question, but it might be more active.

THE CHAIRMAN: I am just wondering whether there is a real problem there or not?

MR. BATES: We do not think there is a real problem. It would be easier for many people if N.H.A. was in the used housing business, but we do not think it is a national problem.

COMMISSIONER MACKINTOSH: Without implying any final judgment would you agree that the case for extending insurance to existing mortgages is stronger as you get into a buyer's market than it was when you had an acute housing shortage, and the emphasis could well be on new housing rather than existing housing? Do you think the scales are tipped a little as you get into a buyer's market?

MR. BATES: Yes, I think the scales have tipped

a little. You have also to consider the other side, what this would mean in terms of government expenditure.

COMMISSIONER MACKINTOSH: I do not mean they are tipped enough, necessarily.

MR. BATES: No.

COMMISSIONER MACKINTOSH: The more you get into that the more consideration might be given to it.

COMMISSIONER GIBSON: It also affects the filtering-down process you were talking about. If you give support to the market for this housing then the accommodation might not be as cheap as it would otherwise have been for people on the lower-income scale. Is that a reasonable statement?

MR. BATES: Yes, I think it would raise the price on new housing; of course it would.

COMMISSIONER BROWN: Has that been the experience with the F.H.A.?

MR. BATES: Well, they were always in it. They were in it right from the beginning.

COMMISSIONER BROWN: Let us put it this way. Do the relative prices of used housing to new housing in the United States differ from the relative prices of used housing to new housing in Canada?

MR. BATES: I cannot answer that question.

COMMISSIONER BROWN: Perhaps Mr. Adamson can answer it.

MR. ADAMSON: I am sorry.

MR. BATES: I do not know what the price of used housing is in Canada, or the price of new housing. You are talking about a mass of things, are

you not? The question cannot really be answered. It is too diverse a population you are speaking of.

MR. ADAMSON: I think there are very strong a priori reasons for thinking that it would put an upward pressure on existing real estate prices. But the mortgage money supplies are completely inelastic it is difficult to see how it could have any major over-all effect other than it would put our present N.H.A. lenders in a position where they could choose wherever they would make their loans. There is no reason to think it would increase their supply of money under the Act unless it were contemplated to change the N.H.A. interest rate.

COMMISSIONER BROWN: We have been told that one objective has been to create a better distribution of existing houses. Would this mean a more economic useful use of existing housing?

MR. ADAMSON: I do not know if it would be more economic, but I think without question it would mean a different distribution of existing units. The very existence of down-payment requirements puts asset holders in a position of advantage in seeking dwelling space, and they are in a position of particular advantage in a used housing market because the cash requirements there are so much greater, relatively speaking. They would lose this advantage if you remove this asymmetry from the market. What this means is that the present twist puts people with assets in a position where they get cheaper accommodation than they otherwise would.

COMMISSIONER GIBSON: Probably the price would be raised to some extent.

MR. ADAMSON: Yes, it would raise the cash price. Again the subjective price to the tenant would presumably be lower. He might prefer to buy a $13,000 house with a down-payment of $500 than a $12,000 house with a down-payment of $2,000. To him, when everything is looked at, it is a cheaper price. The capital price really does not mean anything in abstracto. You have to look at the terms: "I have to pay so much cash out of my jeans, and I get so much from this person" and so on. The capital price might be $12,000 in one case and $15,000 in another. This is not the thing. The capital price does not have a consistent meaning between buyers in different positions.

COMMISSIONER BROWN: Have you any opinion about the sociological position of existing housing, whether this would be improved?

MR. ADAMSON: I do not understand.

COMMISSIONER BROWN: Well, from the point of view of retired people living in houses that are larger than they really need, whereas other people with families are occupying accommodation that is not suitable to them -- would this help to get this accommodation redistributed?

MR. ADAMSON: In the sense that generally I think it would increase mobility.

COMMISSIONER BROWN: In other words, would it further the objective of more equitable distribution

of existing housing?

MR. ADAMSON: Yes. I think it would in part deprive asset holders of an advantage they now have. Asset holders always have an advantage by virtue of having assets, but they have a special one in this case. I do not know whether sociologically that would be a good or bad thing, for I do not know enough about the sociological structure of people who are long on assets or short on assets.

COMMISSIONER GIBSON: I would like to ask one or two questions about the housing policy in its relation to the general economic policy. In the material that you present here, and in your comments, you have left me with the impression that the government-set N.H.A. interest rate is a very potent weapon in effecting the supply of mortgage funds. It looks as though it had been to some extent used anti-cyclically in the past. Certainly the spread between the N.H.A. rate and corporate bond yields was at a low in the boom of 1959 and at a low in the boom of 1956-57. Did this just happen or is this conscious economic policy? You said yourself it is difficult to change this rate and at times when other interest rates are rising if you do not change you get this result. Do you regard this as a proper instrument of economic policy or is it something that just occurs?

MR. BATES: I think it would be very difficult to say that it was a conscious instrument of policy. It may be that all that was considered as part of the over-all policy.

COMMISSIONER GIBSON: It has shown itself to be very effective as an anti-inflationary measure, if you like, because it does cut off the supply of money in this area and, indeed, apparently the supply of all mortgage money to a degree because better yields on corporate bonds, and so on, divert money out of the mortgage market.

MR. BATES: But I think you have always got to remember that the conventional rate can move irrespective ---

COMMISSIONER GIBSON: And does.

MR. BATES: --- and does move irrespective of the N.H.A. rate, so approved lenders may switch from N.H.A. to conventionals, and their judgment there will be related to corporate yields and other factors. Therefore, the potency of this rate is not very great. It did not determine the conventional rate.

COMMISSIONER GIBSON: No. But you see what I am getting at. If the rate is used in this way it is a factor that can be used in an anti-cyclical way from a business and economic policy point of view, but this means it is a factor of instability so far as housing is concerned. It emphasizes the ups and downs and it seems to me that it suggests a certain conflict between the objectives of what you might call the housing policy and the objectives of the economic policy. Is this a real problem?

MR. BATES: Not a major one. It is inherent.

COMMISSIONER GIBSON: Let me put it another way. Is the high degree of instability in the production

of housing, let us say, and in the supply of mortgage funds, a factor in increasing the cost of housing?

MR. BATES: Yes, I would think if the housing industry had a perfectly stable market to which they could adjust themselves, no doubt you would have larger firms emerging, large-scale operations, and constantcy in operations. Many things could happen that could ultimately affect the cost of housing. The housing industry is a very small-scale industry to begin with. People move in and move out. There are not many large builders, and it has always been so. It has been this way in England and in the United States. The costs are dependent to some extent on the amount of productivity that emerges from that sort of industry. Complete stability would no doubt produce larger-scale operators and probably smaller-scale unit costs. I do not know how you can get this in this industry.

COMMISSIONER GIBSON: How about other changes in the terms? You have made it pretty clear here that at times changes in the period of the payment and in the amount of the loan in relation to appraised value have been very important in stimulating the demand for housing and, in 1951 and 1952, in reducing the demand for housing. Do you see these instruments or changes in these terms as significant elements, again in terms of national economic policy in the future? You have made it clear that you think the backlogs have been pretty well made up and that we have gone as far as we can in the amount of loans in relation to the appraised value.

MR. BATES: Yes, you cannot be much more liberal in these terms than you are now.

COMMISSIONER GIBSON: Could they be tightened up?

MR. BATES: They could be tightened up if the occasion required it, just the same as we involved ourselves in rationing in 1960.

COMMISSIONER GIBSON: But the control that was exercised in 1960 was that the government decided to make less money available to C.M.H.C., is that not correct?

MR. BATES: Yes.

COMMISSIONER GIBSON: And we have not used these other instruments for quite a little while in that way?

MR. BATES: This is so but they could be used.

COMMISSIONER GIBSON: Does this make sense?

MR. BATES: Yes.

COMMISSIONER GIBSON: And you do not see any very major problem here in a conflict between housing policy and economic policy?

MR. BATES: Except I do not think you can be much more liberal in housing policy than you are now when you get up to 95 per cent loans.

COMMISSIONER GIBSON: As the person responsible for housing policy do you object to seeing the housing policy used as an anti-cyclical measure?

MR. BATES: Yes.

COMMISSIONER GIBSON: You do?

MR. BATES: Yes, I want to see an adequate volume

of housing coming forward each year.

COMMISSIONER GIBSON: And you would rather not see this used for general economic policy to a major degree?

MR. BATES: Not to the point of sacrificing the shelter needs of the Canadian people.

COMMISSIONER GIBSON: Is this one of the arguments in favour of the fixed rate, of a rate that is changed very seldom, that it automatically produces a certain anti-cyclical behaviour in the supply of N.H.A. funds? If it is not changed, [illegible] and interest rates are rising in a boom, this rate becomes relatively low

and funds are more difficult to obtain; and vice versa; when interest rates are going down, this interest rate gets relatively high?

MR. BATES: That is what is happening, yes.

COMMISSIONER GIBSON: Is this a good thing; that is what I am getting at?

MR. BATES: Is this a good thing, sir?

COMMISSIONER GIBSON: Is this a strong argument in favour of a relatively fixed rate?

MR. BATES: It is an argument in favour of a relatively fixed rate, yes.

COMMISSIONER GIBSON: Do you think it is an important argument?

MR. BATES: No, but it is an argument.

COMMISSIONER GIBSON: In other words, you would put housing policy first as you [illegible] in your thinking, to get a reasonably good supply of housing?

MR. BATES: This is my job.

MR. ADAMSON: Not just a fixed rate, but also a low rate, because the capacity to control demand on mortgage loans in this field depends on the N.H.A. terms being a bargain, which is not

always available. The more of a bargain it is, the more excess demand you have that you can release when you want to release it.

COMMISSIONER GIBSON: But if a market is going up, your rate then becomes low and there is very little interest from the standpoint of attracting mortgage funds?

MR. ADAMSON: Yes; but today conventional rates and N.H.A. rates are reasonably close together so that the N.H.A. does not constitute as much of a bargain. We clearly do not have the excess demand to make N.H.A. money available to any mortgagor who wants to borrow it, as we would if the N.H.A. rate were lower. This was a decisive point in the market in 1957. We had a much greater demand than we have today. I think this is the point. The possibility of doing this is not as great as it was throughout most of the fifties.

COMMISSIONER GIBSON: And if you want to make the rate a factor in the demand, from the standpoint of the person buying the house, this means that the government has to put up the money as the private suppliers leave the market, and if the government cannot put up the money, the low rate restricts housing activity?

MR. BATES: This is so, sir.

COMMISSIONER GIBSON: I was thinking rather the other way, of a low rate restricting housing activity in booms, and because a fixed rate would tend to be relatively high in a recession, encouraging housing

activity in a recession.

MR. ADAMSON: This was basically the rough pattern during the fifties. This tended to happen. Although the anti-cyclical behaviour of housing in total has been something less than perfect, there has been some tendency for starts to start rising rapidly when general money interest rates were declining.

COMMISSIONER LEMAN: Is Mr. Gibson through on that point?

COMMISSIONER GIBSON: On that particular point, yes.

COMMISSIONER LEMAN: I wanted to go into another area, Mr. Chairman.

THE CHAIRMAN: All right.

COMMISSIONER LEMAN: We have heard from other people who came before the Commission, and although I admit that at the time they were making these points about the various provincial laws regarding foreclosure procedures, et cetera, they were then talking mostly in the area of creating a secondary market for mortgages, but just as a preliminary to talking about secondary markets, could you tell us if C.M.H.C. has encountered difficulties related to these legal differences in procedures for the administration of mortgages, including foreclosure.

MR. WILSON: It is a difficult thing to decide in itself, because it depends on degree. We certainly find that we have more administrative troubles in the province of Alberta than we do in Ontario, because

much more legislative protection to the borrower is given in Alberta than is given in Ontario. This may account for the rather unusually high proportion of N.H.A. direct lending in Alberta. It may be that other people do not like Alberta because of this. We certainly find in our experience that we have more difficulty there.

We have a bit more trouble in Quebec, not because of the legislative difficulty but because of what you might call the inertia of their court proceedings and the additional time it takes to go through the procedure, although the relative laws are roughly comparable as between Quebec and Ontario.

Apart from these two provinces there does not seem to be any variable degree of difficulty in terms of foreclosure procedures.

COMMISSIONER LEMAN: Has this meant any particular regulations under the Act which you have had to put in?

MR. WILSON: Except for the prohibition of farm loans in Saskatchewan, which were subject to an absolute moratorium at the time, I do not think there has ever been anything like a prohibition or a restriction on willingness to lend anywhere in Canada under the National Housing Act.

COMMISSIONER LEMAN: What I am driving at is this. Does it influence the adequacy of the insurance?

MR. WILSON: No, because the insurance is payable only after foreclosure. It depends whether

you are looking at adequacy from our point of view or from the point of view of the lender.

COMMISSIONER LEMAN: From the point of view of the lender.

MR. WILSON: From the point of view of the lender, it might. The insurance provides a lender, for practical purposes, with insurance for a period of about eighteen months after default before he suffers what you might call a decline in effective return. So if a foreclosure can be accomplished within eighteen months, on an average, the insurance is 100 per cent insurance.

I doubt that a lender could demonstrate that, on averages, even in Alberta or Quebec, this does not constitute 100 per cent insurance at the present time.

COMMISSIONER MacKEEN: Mr. Wilson, do you have the personal covenant of the borrower in Alberta?

MR. WILSON: In terms of our direct loans?

COMMISSIONER MacKEEN: On direct loans.

MR. WILSON: We have a covenant of the borrower on any loan, but to the extent that you may have to choose between the covenant of the borrower and the value of the property, we have always chosen the value of the property, to date.

COMMISSIONER MacKEEN: Conventional loans are not covered in Alberta by the personal covenant, are they?

MR. WILSON: I do not know. N.H.A. loans are covered to the extent that you seek to go to the property for your security, so that I would say, in that sense, neither conventional or N.H.A. have that protection.

COMMISSIONER LEMAN: All N.H.A. housing loans are made on what is commonly called the blended payment system, are they?

MR. WILSON: This is a mortgage administration procedural distinction. Most of the lenders do their accounting on what is called the blended system. There are a few lenders, and we ourselves as lenders, who use the flat rate payment system. There are some of the approved lenders who use the same system. If you talk in terms of blended payments of principal and interest, all of them are on that basis.

COMMISSIONER LEMAN: In case of a need for a moratorium fairly early in the curve, a moratorium on the principal, there would be not much change in the monthly payments that have to be made?

MR. WILSON: This would depend on when in the amortization table --

COMMISSIONER LEMAN: I say, early in the curve.

MR. WILSON: Early, they would be comparatively small.

COMMISSIONER LEMAN: So you regard as invalid any claim by lenders that there is some defect in the adequacy of the insurance from their point of view?

MR. WILSON: If their point is that it is

not insurance against moratorium legislation, their contention would not be invalid. Mortgage loans insurance is not insurance against provincial moratorium legislation. I do not know whether any government could attempt to take issue with other governmental action. Certainly if any province passed absolute moratorium legislation, lenders would be caught with that.

COMMISSIONER MACKINTOSH: I would like to direct some attention to what you have to say about the secondary market. You indicate in the quotation, I think, from your annual report that there has been slow but sure progress in this over the last eight or ten years, and that the major steps in it have come as a result of your auctions.

Would you tell me, just so I can get a more realistic view of it, on what basis institutions bid and what actually is the auction procedure?

MR. BATES: The auctions began last year and we have no great experience yet. The procedure is to send out lists of mortgages in different parts of the country, giving the streets -- not the names of the people; we felt we could not go quite so far as that, but giving the streets with the particular blocks of mortgages that we put together.

These are put together on a basis that allows a bidder to select from Nova Scotia, Guelph or western Ontario, or somewhere else. These lists are sent to all the approved lenders and the investment dealers in Canada. They are asked to bid on these.

COMMISSIONER MACKINTOSH: May I interject there? As I understand it, if they buy, they buy a package?

MR. BATES: Yes, sir.

COMMISSIONER MACKINTOSH: Do you make the package, or do they make the package?

MR. BATES: We make the package, and we offer these different packages for their consideration. In the package there is a quarter of a million, up to half a million packages. Maybe in the future we will have to cut them down a little bit. Maybe we will make them bigger, wider than they are; but our process here has been really to test the market and see what sort of offers would come forward.

We have had five auctions, including the last one. The last one was a flummox; it came out the day the government announced some problem of austerity. So we have had four auctions. Whether or not the auction technique is the best, we have still to learn, and consideration is being given at the moment to listing offers at posted prices so that an investment dealer may be able to come along and say, "We will buy $1 million at that price and we will go out and sell bonds on the market for $5 million. Hold this for me for the next three months". Under the auction technique this is difficult for that type of firm, because they do not know whether they are going to win the bid or not. So at present the subject is being considered by a committee of three, the Deputy Minister of Finance, the Governor of the

Bank and myself, who are responsible to the Minister of Finance and the Minister of Public Works for advising them on the development, the attempted development of this market. The committee is considering this question of posting bids as well as the method of auction.

COMMISSIONER MACKINTOSH: That is to say, they can bid at any time?

MR. BATES: Yes, we would stand ready, say for a month, to offer up to any amount at 6 3/4 or 6½ at such and such a price.

COMMISSIONER MACKINTOSH: An elementary question. What is the form of their bid? You say you offer this parcel of mortgages for a certain principal sum.

MR. BATES: Each time so far that we have offered parcels, they were all at the same rates; that is, they were either 6 per cent mortgages or they were 6 3/4, so the bids would simply come in at 101 or 101.5; or in the case of 6's they would come in at somewhere in the 90's.

MR. ADAMSON: Bids specific to each parcel.

MR. BATES: Yes. And these bids varied according to the buyers' estimates of whether they wanted to hold mortgages at Sydney, say, distinct from Scarborough, Toronto.

COMMISSIONER MACKINTOSH: Distinct as above and below par?

MR. BATES: Yes.

COMMISSIONER MACKINTOSH: We can assume, I

imagine, that you want to get the best price possible. Do you clear the market on these auctions, or do you reject bid as being too low?

MR. BATES: Yes, we do not necessarily take all the bids. We have taken -- when selling high price mortgages you expect a substantial premium. If we are selling 6's you expect some reduction below par.

I will read the figures to you, sir, which have just been given to me. The 6 3/4 stuff, the average price of the first one was 101.17, then 101.35, and then 101.79. When we sold the 6's in March, it was 97.60.

COMMISSIONER LEMAN: What information does the bidder have, again? He has the streets, et cetera. Does he have information on the collection experience, et cetera?

MR. BATES: No, sir. There is nothing in the parcel that is in arrears at the moment the bid is made. In other words, we do not offer any particular house with regard to which the home owner is in arrears. Of course, they are all insured loans.

COMMISSIONER LEMAN: There is no general statement that on this package collection experience has been satisfactory.

MR. BATES: Well, it is an indication that there is nothing in arrears.

COMMISSIONER MACKINTOSH: How satisfied are you with the distribution resulting from these auctions?

MR. BATES: Satisfied of what, sir?

COMMISSIONER MACKINTOSH: The distribution.

MR. BATES: Do you mean, among buyers?

COMMISSIONER MACKINTOSH: Yes.

MR. BATES: Experience is still quite limited. We have had buyers from chartered banks, trust companies and investment dealers. In other words, there is some wide distribution among the institutional buyers.

COMMISSIONER MACKINTOSH: Most of your buyers have been the approved lenders?

MR. BATES: Including investment dealers who are not approved lenders; in other words, we opened the market to the investment dealers of Canada who are not approved lenders, generally.

COMMISSIONER MACKINTOSH: The banks, I take it, might feel they could buy the 6's at a discount and put themselves in a slightly more legal position than if they were making new loans under a 6 per cent ceiling. Is that a factor?

MR. BATES: This is no doubt a factor. They could buy $6\frac{3}{4}$ because this is an investment they were making, and the 6 per cent ceiling on their loans didn't apply.

COMMISSIONER MACKINTOSH: While this may not be comprehensive, I would see approved lenders might by this means shift their portfolios: get more mortgages here and less there, and so on. But the contribution to the increase in the market would, I suppose, depend on these buyers at the auction distributing a certain part of their purchases to institutions or funds or individuals who otherwise would not have access to N.H.A. mortgages? This is what I mean by distribution.

MR. BATES: Well, I think this is so. After all, most of the approved lenders have the machinery

for making their own loans. They have got the overhead there and they want to use it. Naturally, in the various auctions most of the banks and trust companies who bought were buying for pension funds, not really for their own portfolios.

COMMISSIONER MACKINTOSH: Here again, to go back over earlier ground, is a place where the demand is greatly affected by the fluctuation of rates in that these mortgages are attractive to pension funds at certain times, and at other times, as against bond rates, are relatively unattractive?

MR. BATES: Yes.

COMMISSIONER MACKINTOSH: There is some presumption that distribution might be more continuous if the mortgage rates fluctuated with the market rates rather than being adjusted only sluggishly; isn't that true?

MR. BATES: I think I might mention too there are at least two, perhaps more, new institutions which have been set up by private enterprise, and their intention is to sell their own debentures -- small pieces -- and to hold in their assets the insured mortgages. This means that a small man, or woman, with $1,000 can buy a debenture in a company that is secured by an insured mortgage. This is really a new type of institution in the Canadian capital market and, of course, it is where in institutions like this that the question of posted prices and the availability of funds becomes most important.

COMMISSIONER MACKINTOSH: But the difference

is only in the insured mortgage. There have been for a long time institutions who sold debentures against mortgages.

MR. BATES: Yes, quite.

COMMISSIONER MACKINTOSH: Do you think that is the way in which the small investor, who does not want the bother of looking after mortgages but who would like the mortgage rate, can get in this market?

MR. BATES: And the government guarantee.

COMMISSIONER MACKINTOSH: Yes.

MR. BATES: And the government guarantee, yes.

COMMISSIONER MACKINTOSH: And that that is the better route, and not having the people who buy at auctions getting down into a small retail business of selling the small investor two or three mortgages?

MR. BATES: Yes. This makes the whole thing much more flexible. A widow with $1,000 can enter the insured mortgage market this way.

COMMISSIONER MACKINTOSH: Through the debenture?

MR. BATES: Through the debenture.

COMMISSIONER GIBSON: Does the coupon interest rate on mortgages which you put up for auction make much difference? Are some much more attractive than others, or do they bid prices according to the current market?

MR. BATES: They simply bid according to the current market.

COMMISSIONER GIBSON: So it doesn't matter too much what the coupon rate is?

MR. BATES: No. It matters to me, though.

COMMISSIONER BROWN: Wouldn't it matter in this sense, that the high coupon ones are above par and, therefore, are more subject to call in the sense of being repaid on a change of interest rates than the 6 per cent ones selling below par?

MR. BATES: Yes, this is a danger. This question of call is always there.

MR. ADAMSON: The discount paper is far more attractive to the market.

COMMISSIONER BROWN: Yes.

COMMISSIONER GIBSON: Yes, but the market would take account of these factors?

MR. BATES: Yes, of course.

COMMISSIONER MacKEEN: You suggested that there was a difference in the rate between regions: you mentioned Sydney and Toronto. Why should that make very much difference in an insured mortgage which is virtually a government guarantee?

MR. BATES: That is a very good question. We don't think there should be any difference, but there is. The buyers reflect different judgments. We think they are all the same; they are all 100 per cent guaranteed; but, this is the fact. Maybe the buyers think there is more danger of foreclosure problems in some areas than in others.

COMMISSIONER MacKEEN: How much of a problem is that to the buyer? Don't you handle that?

MR. BATES: Yes.

COMMISSIONER MacKEEN: It doesn't put him

under any strain?

MR. BATES: No.

COMMISSIONER GIBSON: But mortgages in certain places in these packages sell for better prices than mortgages in other places; this is true, isn't it?

MR. BATES: This is true, yes.

COMMISSIONER GIBSON: If you had a free N.H.A. rate, would you expect to see important differentials?

MR. BATES: This would make no difference to that.

COMMISSIONER GIBSON: But the rate may be different in one area from another, then?

MR. BATES: You are thinking that if we had a free rate it would be higher in Sydney than in Toronto, anyway?

COMMISSIONER GIBSON: Yes. What sort of differences would you expect in a free rate situation?

MR. BATES: I suppose the same as a conventional mortgage, pretty much -- I don't know.

MR. ADAMSON: There should not be quite that much because of the blanket coverage.

COMMISSIONER BROWN: As the money that is coming from investors in purchasing these mortgages is presumably being diverted from some other potential investment, have you any theories as to what areas are receiving less investment?

MR. BATES: No, we really don't know. We know some of the buyers who are buying for American insurance companies. This may have been an addition

to Canadian capital. Some were buying for Canadian pension funds which might otherwise have bought corporate bonds -- I don't know.

COMMISSIONER BROWN: There is no study as to whether this money might otherwise have gone into government bonds or conventional mortgages?

MR. BATES: I don't think some of the buyers would know, themselves, what might have been done with the money in the pension fund for which they are acting as trustee.

COMMISSIONER MACKINTOSH: I would think there is a likelihood that in a fund whose liabilities were very long-term, like a pension fund, that there would be consideration of the two securities which carry the credit of the federal government, and whether the requirements of the pension fund are equally well met by a guaranteed mortgage as against a bond which in recent years has been subject to some rather drastic fluctuations. I take it that you, subject to a variety of problems, think there is probably a considerable future for the debenture-issuing mortgage corporation?

MR. BATES: I think so.

COMMISSIONER MACKINTOSH: That this is an institution that fits into the developing patterns...

MR. BATES: Of the capital market.

COMMISSIONER MACKINTOSH: And ought to be encouraged?

MR. BATES: Yes.

COMMISSIONER MACKINTOSH: You raise a related

matter: you have, I think, in the C.M.H.C. Act authority to act as a lender of last resort; I forget whether it is limited to the approved lenders under the Act or not. This power, I understand, has never been used; is that right?

MR. BATES: I think it was used once before my time. It was used once, I believe. You mean lending to an approved lender?

COMMISSIONER MACKINTOSH: Yes.

MR. BATES: Yes, it was used once.

COMMISSIONER MACKINTOSH: The power is there: is the machinery set up? If an approved lender comes forward and wants to borrow, has the Corporation got a procedure and standards under which they would lend if they felt it were desirable?

MR. BATES: I think we would require, really, to get a judgment from government on this because of the fact that the power has really never been used. It is a power of considerable importance. It is not something that you would look at as a kind of automatic thing you would do, anyway, because it happened to be in the Act. I think we would have to get a declaration of government policy to us on this point, because it could conceivably involve us in quite substantial lending.

You can easily see in this secondary market that if one of these new types of institutions bids or offers to buy a substantial quantity of mortgages and then finds they cannot finance them, if we were using this power it would be very nice for them to come

to us and say, "Please lend on this". Or, if they were borrowing short during the first period, while they were buying, and something happened to the short-term market, it might be very nice for them to come to the corporation and say, "Could you lend us this -- it may be at a prohibitive rate for a week or two weeks -- until we can get other accommodation?" This power is there, but in order to use it in this sort of way we would really require to get governmental authority.

COMMISSIONER MACKINTOSH: Yes, I recognize that, but there is the other question: suppose this happens, are you in a position to advise the government? Have you thought out the problem? This has been represented to us as being essential to the further broadening of the secondary market.

MR. BATES: I am not quite clear what you mean -- am I in a position to advise the government? I am always in a position to advise the government. I think we could advise them in terms of principle, but certainly not, sir, in terms of details, no. We haven't thought it through to that point, because the question really has not come to us.

COMMISSIONER MACKINTOSH: Well, the presumption presented to us has been that probably such credit would be available only at a penalty rate?

MR. BATES: Yes, of course.

COMMISSIONER MACKINTOSH: If you have some companies in this field and they go ahead and then need this temporary assistance, it is not an entirely

satisfactory answer to say that the government will take it under consideration and some time in the next eighteen months will produce an answer, because if they apply it is probably because of an impending need of some urgency.

MR. BATES: Well, all I can say is that the question has not arisen, and quite clearly it is not one that would be determined only by C.M.H.C. The Department of Finance and the Bank of Canada would both feel they had important things to say about it.

COMMISSIONER MACKINTOSH: We even had a suggestion that C.M.H.C. should always have a bid and offer in the secondary mortgage market.

MR. BATES: We should always have a bid and offer?

COMMISSIONER MACKINTOSH: Yes. In effect, be the Bank of Canada for the mortgage market, run an active purchase and sale operation on both sides of the market. Naturally, we haven't formed any views on this. If you have any, I would welcome them.

MR. BATES: If you are asking me, Dr. Mackintosh, as a bureaucrat if I would like to expand my empire, the answer is yes.

COMMISSIONER GIBSON: On the same subject, one of the other things that has been represented to us is that N.H.A. mortgages are somewhat unsatisfactory instruments because nobody knows what the term is. There is the repayment privilege which starts after three years, I think?

MR. BATES: Right.

COMMISSIONER GIBSON: Now, this is thought by many to complicate the matter of marketing, particularly of instruments based on a portfolio of mortgages. Is this important to the persons getting the mortgage money? Is it of much significance?

MR. BATES: This right to repay?

COMMISSIONER GIBSON: Yes, the right to repay: is it regarded as something important by the persons getting the mortgage money?

MR. BATES: Yes. If they die and leave the daughter $5,000, she may want to pay off $5,000 on the mortgage: why should she not do so?

COMMISSIONER GIBSON: There is no penalty, though, or anything?

MR. BATES: No, not after three years.

MR. WILSON: Just the usual three months interest, that is all.

COMMISSIONER GIBSON: Do you think that that is an important enough matter to consider possibly varying to some degree the repayment privileges on these mortgages to make them more marketable instruments?

MR. BATES: I think that the buyer takes this into account when he is buying mortgages; he knows that there is an uncertain period in it.

COMMISSIONER GIBSON: That is one of the problems which anybody thinking of setting up a mortgage company and putting out obligations against first mortgages has to worry about?

MR. BATES: Yes. It is a difficult problem, but we don't think we should force the borrower to hold a mortgage which he or she doesn't want.

COMMISSIONER GIBSON: There could be larger penalties; the right to repay would come after five years instead of three. I am not suggesting it, I am merely saying that there is a lot of ground here that we might explore if it were thought worthwhile.

MR. BATES: If it were a real impediment to the market we might have to look at it, but it doesn't seem to be. Whoever you are, when you buy a mortgage each month you are getting repayment of principal and interest on it and you have this principal problem in front of you for the whole 25 years; some of it coming in every month and it gets bigger and bigger and it has to be reinvested somewhere, and you are up against this problem anyway so the call

privilege doesn't apply.

MR. ADAMSON: And it affects the calculation of yield on the basis of which the buyer bids in that it introduces an element of an absolute indeterminary, which is not characteristic in this form of other kinds of investment. ... Presumably this had some influence and was of some benefit to the borrower.

COMMISSIONER GIBSON: Thinking in terms of investments, insurance companies, for example, are generally interested in rather long-term, whereas banks and loan companies and trust companies are interested in short-term obligations. Is there some way of selling the long end to an insurance company and placing the short end with a loan company? There may be some possible ground for exploration here, but you can't do that and have the repayment privilege on it.

COMMISSIONER LEMAN: To get this in perspective, why don't we ask what has been the experience on accelerated repayment of N.H.A. loans?

MR. ADAMSON: That is a young portfolio ---

MR. BATES: Most of the loans have only been since 1957. It is quite a young portfolio, although it is very large. The repayments, I think, have been very small; I just don't know offhand.

COMMISSIONER MACKINTOSH: Do your approved lenders ever tell you what their experience has been? Some of them have been in quite a while.

MR. WILSON: They report repayments annually;

they report any balances.

COMMISSIONER LEMAN: Have you any figures on this?

THE CHAIRMAN: These can change quite considerably if interest rates change?

MR. WILSON: Yes.

THE CHAIRMAN: And if conventional mortgages went down to, say, 6 per cent or 5¾ per cent, you could have some of the present loan repaid.

COMMISSIONER GIBSON: And this would be over the life of the N.H.A. mortgage, over the period of your operations?

MR. BATES: The figure in my mind is fourteen years, somewhere around fourteen years on a 25-year loan; the average is about fourteen years.

COMMISSIONER GIBSON: Mr. Brown said, of course, that it could vary, but this gives some idea.

MR. ADAMSON: Certainly in terms of the contractual requirement of the mortgage this is a very large amount; presumably it is a 25-year amortization, but it almost never happens.

COMMISSIONER LEMAN: In corporate bonds there are two types of restrictions that can take place; the right of repayment with a premium or penalty, and also sometimes you can get, say, a 10-year non-refunding clause, that you can't repay the debt for refunding purposes, would that be impracticable in the residential mortgage field, that no new N.H.A. loan would be granted to a person who had just paid off a loan?

MR. BATES: Why would you do it? Nobody wants it particularly.

COMMISSIONER LEMAN: Perhaps people would want it, those who think that this question of maturity is important to them, that that is a problem to them as lenders.

MR. BATES: As lenders.

COMMISSIONER LEMAN: They might think it is important to have some kind of a system of protection against refunding, you say?

MR. BATES: It is not impossible, no.

COMMISSIONER LEMAN: Do you see any great administrative difficulties in introducing such a non-refunding clause for a longer period than the three years which you have mentioned on the straight right to repay?

MR. BATES: It is our job to overcome these difficulties. They are not administrative; they may be political ones, but never administrative.

THE CHAIRMAN: These are very long-term mortgages in the sense of 25 years. Has there been any consideration to having a higher penalty when it is repaid in the earlier years?

MR. WILSON: No, because of the provisions of the Interest Act, which permits repayment without penalty beyond an interest bonus, so at the moment under the present legislation you might increase from the present three to a maximum of five with the

exception of corporate borrowers. The N.H.A. with corporate borrowers does permit a longer built-in term. This applies only to rental housing loans.

COMMISSIONER MACKINTOSH: What is the usual use there?

MR. WILSON: Ten years.

COMMISSIONER MACKINTOSH: And then what is the penalty?

MR. WILSON: After ten years there is a three months penalty. Actually, without consent the borrower has no right to repay.

MR. ADAMSON: The borrower might become interested in this if the question were asked, "How interested are the lenders? Would they make a loan for a lower interest rate?" Then there would be something in it for the borrower, too, and he could judge whether he wanted to be tied in for 25 years at a rate of 'X' / or have considerable freedom at a rate of X plus something. There is no point in replacing one kind of rigidity with another.

COMMISSIONER BROWN: Would you have a conflict with the Interest Act as far as individuals are concerned?

MR. ADAMSON: Yes you would; beyond five years there is nothing we can do.

COMMISSIONER BROWN: This has been brought up because we had had it mentioned by a number of would-be lenders that this is a factor, why they are reluctant to loan under N.H.A.

MR. ADAMSON: There is really not much room there between what the Interest Act requires and what our Act requires.

MR. BATES: It can't make much difference.

COMMISSIONER GIBSON: For the purposes of the record, you said that the average mortgage outstanding ran about 14 years; is that the time on repayment or is that the average period that a 25-year mortgage, being paid out in instalments over the period, would work out too?

MR. ADAMSON: No, that is the number of years which the contract would be outstanding.

COMMISSIONER GIBSON: It would be all cleaned up at the end of 14 years?

MR. ADAMSON: Yes. I think even if it goes for 25 that you get a figure of something like 16 on the average.

COMMISSIONER GIBSON: One other question on this secondary mortgage market. Why go to all this trouble for C.M.H.C. direct lending; why doesn't the government just issue bonds? Why go to all the trouble of establishing this market and selling your special N.H.A. mortgages for the purpose of your lending?

MR. BATES: That is what it does, we are ---

COMMISSIONER GIBSON: You are trying to pay them back, though, by developing this instrument and getting it on the market?

MR. BATES: But the purpose of selling this is not to repay.

COMMISSIONER GIBSON: To limit the amount of government participation?

MR. BATES: No, to see if a fluid market can be set up in mortgages. It is true that when we sell a mortgage we repay the debenture that we already have from the government; we simply repay it.

COMMISSIONER GIBSON: All I am saying is it worth all the effort from your point of view?

MR. BATES: Well, it is not much effort. One man in the corporation issues an auction every two or three months to see if you can get an increased flow of funds, whether it is from the American pension funds or somewhere else; it is not costing us very much.

COMMISSIONER GIBSON: Another way of putting it is would it be more economical simply to talk in terms of the paper being issued as being government bonds, and they sell at higher prices with lower yields?

MR. BATES: I see what you mean.

MR. ADAMSON: It is an expensive way of borrowing money. These mortgages are sold to yield what? Well over 6.

COMMISSIONER GIBSON: That is the point.

MR. ADAMSON: As far as being a device to obtain government funds is concerned it is an expensive way of doing it. It is to develop an appetite or to familiarize pension funds and other people in this so that they might in time have a greater demand.

COMMISSIONER MACKINTOSH: Surely the answer is that if your only purpose in this operation was to recoup your own funds, it wouldn't be worthwhile?

MR. BATES: No, quite.

COMMISSIONER MACKINTOSH: What you pay for is this future benefit that is presumed to develop to the secondary market?

MR. BATES: Yes, and it is not costing us very much.

COMMISSIONER LEMAN: Are you through on that subject, Mr. Gibson? Under what conditions and on what terms can a mortgagor get off the covenant on an N.H.A. loan, or can he at all?

MR. WILSON: For practical purposes, as the soon as the foreclosure takes place and the lender acquires the profit on an N.H.A. loan, if he elects to realize on the insurance he must turn the property over to us as a condition precedent to payment. This makes us a third-party purchaser, and as soon as the lender surrenders the authority to re-convey the property to the original borrower, he loses his ability to exercise any collection on the personal covenant.

COMMISSIONER LEMAN: But are you not subrogated in his rights?

MR. WILSON: It might be possible for the lender to obtain a judgment in debt rather than a foreclosure, and then assign that judgment to us. We have relied on ordinary foreclosure procedures, which basically produces the property as security

rather than the personal judgment as security.

COMMISSIONER LEMAN: Well, that doesn't directly answer my question. Are there conditions and terms under which C.M.H.C. would let off the mortgagor, the earlier mortgagor?

MR. WILSON: And release the covenant?

COMMISSIONER LEMAN: Yes?

MR. WILSON: It is permitted by the regulations where the original covenantor was a builder, providing the builder obtained the assumption of liability by the purchaser and the purchaser has a gross debt service ratio that is acceptable and pays the minimum down-payment, and so on. That is the only provision in the regulations for a specific lender, by operation of law, to release a covenant.

COMMISSIONER BROWN: The individual home owner cannot cut off when he sells the house?

MR. WILSON: Except by operation of law, to the extent that that occurs.

COMMISSIONER LEMAN: Automatically he should keep this as a contingent liability?

MR. WILSON: If he keeps that kind of a balance sheet, yes.

COMMISSIONER LEMAN: He might have to make one up to get a loan, for instance.

COMMISSIONER BROWN: What happens if he dies?

MR. WILSON: Presumably this would be an equal contingent liability in terms of his estate; the estate is normally not tied up. I believe -- and I am not sure I am accurate on this -- I believe

we have had occasional requests for a release of covenant in terms of our direct lending from an estate of a person who has sold the property for purposes of clearing the estate, and I believe we have on occasion given such a release under the circumstances.

COMMISSIONER BROWN: Do the other lenders holding the mortgages have the power to give such a release?

MR. WILSON: I think they could do so under the regulations only with the approval of the Corporation.

COMMISSIONER BROWN: This hasn't arisen?

MR. WILSON: I can't recall it ever having arisen.

COMMISSIONER LEMAN: Suppose that the lender foresees that he has to go through foreclosure proceedings, but he finds in the title a very good credit, wouldn't it be cheaper for him to go to that very good credit and obtain his money rather than go through either the insurance or the foreclosure himself.

MR. WILSON: Firstly, it would have to be a very good credit indeed and one that was better than a 100 per cent guarantee.

COMMISSIONER BROWN: On home improvement loans, which at the moment, as I understand, are limited to $4,000 and a ten-year term, we have had representations that those should be doubled both as to amount and as to term. Have you any comments to make on this?

MR. BATES: This, of course, would be a matter

of government policy which would require a change in the Act. I think that the average runs about $2,500 or less than that, so that this present maximum is not too much of a restraint in the sense that the loans which are made by the banks probably are as high as the banks intend to make them anyways, but certainly a longer period and a bigger loan would probably permit rehabilitation operations in housing that are highly desirable in many instances. Now, whether the banks would grant it, I don't know. Theoretically, $4,000 is not enough to do a job on a duplex or a quadruplex, or what have you; it might be quite desirable to have a larger figure and banks in some instances might be prepared to go ahead with bigger loans, but the average loan is $1,300.

COMMISSIONER BROWN: Is that average tending to increase?

MR. BATES: No.

COMMISSIONER BROWN: That is the average loan when originally made, not the average outstanding?

MR. HIGNETT: When originally made. In 1961 there were 26,900 loans made for a total amount of $39 million.

MR. BATES: It was raised a few years ago and it made very little difference to the actual size of the loan. My recollection is that we changed the Act from two to four, didn't we?

MR. HIGNETT: From $2,500 to four.

MR. BATES: From $2,500 to $4,000, but it made no difference in the size of the loan. This may

due to demand factors as distinct from supply factors, I don't know.

COMMISSIONER BROWN: There is one other question which I would like to have your opinion on, and that is what would be the effects on the mortgage market and the availability of mortgage funds if the banks were permitted to go into the conventional mortgage field to some degree? This, of course, would involve other changes as well.

MR. BATES: Yes.

COMMISSIONER BROWN: Let us say that all these changes were made.

MR. BATES: You mean, allowing them to make loans above 6 per cent?

COMMISSIONER BROWN: Yes.

MR. BATES: This would be very significant and highly desirable. I don't see why the banks couldn't go into the mortgage business if others are going into the banking business.

COMMISSIONER BROWN: Presumably, of course, this would mean that the banks would have less money available for other purposes?

MR. BATES: Yes.

COMMISSIONER BROWN: It would have to come from some other sectors of the economy?

MR. BATES: But from where we sit, we don't care whether they can get N.H.A. or conventional loans so long as they get into the mortgage business and stay in it!

COMMISSIONER BROWN: I am afraid that that is

probably the answer that I expected.

THE CHAIRMAN: Thank you very much, gentlemen.

MR. BATES: Do you require us again?

THE CHAIRMAN: No, I think that is it for the time being.

MR. BATES: Thank you, sir. I was a pleasure to be before you.

THE CHAIRMAN: It has been a very great pleasure for us to have had you with us and to have taken part in this stimulating discussion.

We shall adjourn now until 2.30 this afternoon when we shall hear the brief of Mr. David Mansur.

--- Luncheon Adjournment.

--- On resuming at 2.30 P.M.

SUBMISSION OF

MR. D.B. MANSUR

THE CHAIRMAN: Mr. Mansur, we welcome you as a witness before us today. We have read your brief with great interest and there are a number of questions we would like to ask. I do not know whether you had intended to make any preliminary statement, or whether you wish us to proceed immediately and pursue our questions.

MR. MANSUR: I think not, Mr. Chairman, except to say one thing. I have read the evidence that has been presented to this Commission and have listened to some of the comments, and read some of the transcripts. It seems to me that the problem before the Commission in this field falls into three main categories and everything ---

THE CHAIRMAN: You may sit down, if you would feel more comfortable.

MR. MANSUR: Thank you very much, Mr. Chairman. It seems to me that the evidence heard by the Commission to date falls into three main categories. The first is -- not necessarily in order of importance -- the difficulties about financing existing housing. The second is the flow of mortgage funds, and the third are the factors relating to effective demand.

I think just about everything that has been said will fall into one of those categories, but having

said that, Mr. Chairman, I immediately want to say that in most of the discussion there has been quite an interplay between the economic implications and the social implications. Practically everything that has been discussed has social connotations and financial connotations, and sometimes they do not lead to exactly the same conclusion.

That is all I have to say, Mr. Chairman.

THE CHAIRMAN: I would like to begin by asking a few questions under your heading, "Financing Sale of Existing Houses". I have to leave a little early today, so I am going to take this out of order, if you do not mind. This is at page 9. You begin by saying:

> "Perhaps the most important gap in our mortgage lending pattern is the lack of crisp and identifiable means of financing to facilitate the transfer of an existing house from a willing vendor to a willing purchaser at a mutually satisfactory price."

Do you think it would be possible under any circumstances to design a lending pattern which is a crisp and identifiable means of transferring existing houses?

MR. MANSUR: Perhaps, Mr. Chairman, the phrase would have been better as "crisper and more identifiable means". That would perhaps be a better way to express the thought. But the circumstances vary so greatly that although we talk generally about the financing of existing houses, if we go the full range of the spectrum

I might just mention what I think are the three main categories in it.

First there is the sale of the house in the newer areas. By "newer areas" let us talk post-war sub-divisions, 1945 and on, in which the lending institutions will operate very freely, so that there is no problem really in that area of finding a 66-2/3 per cent mortgage. Just what that 66-2/3 is of, I am not clear, notwithstanding evidence you have heard about the firmness of appraisals.

Then you move into the second sector, which might be the 1920 to 1939 housing. In Toronto it would be, say, south of St. Clair. In Vancouver it might be first Shaughnessey and the better parts of Grandview. In Calgary, the lower part of the North Hill. These are the areas where some of the lending institutions are making first mortgage loans for two-thirds, generally with an interest rate rather higher than the conventional loans in the more preferred areas.

Then you move into the third area, where the lending institutions will not operate, except in the most exceptional cases, even at an increased interest rate. They are just not interested. By this, I mean the core of the cities. I would say that in Toronto almost everything south of Bloor Street fell into this category. In Calgary, probably the east end and Ogden. In Vancouver, everything below 16th; or anything north of 16th/it would be very difficult to get a lending institution to make a loan on at all.

So I suggest there are these three

separate and distinct parts of this financing of existing houses, each one of which carries rather different implications.

As to finding a method of doing this, there have been references before this Commission to the F.H.A. It is perfectly true that the F.H.A. makes twice as many loans on existing houses as they do on new houses, but the F.H.A. operates their existing houses selection with an eye to insurance risks involved. Generally speaking my observation in the United States would lead me to believe that the F.H.A., were it operating in Canada, would operate only in area No. 1, with very few excursions into area No. 2 and no excursions at all into area No. 3. There have been attempts by the subsidized housing group in the United States to get the F.H.A. to use its lending on existing houses to assist the rehabilitation of the older down-town areas. There has been the odd case where this has been done; but generally speaking the F.H.A. selection as to risks is just about as firm in respect to existing houses as it is to new houses. I admit quite frankly, Mr. Chairman, that an F.H.A. type of operation would relieve the problem of area No. 1, but that is not the area in which the problem we now face is most acute. It is most acute in areas 2 and 3.

Therefore one would have to devise something other than bringing the N.H.A. into the existing house field. I think there are ways and means of doing it,

but I think they are all pretty complicated; they are all costly. There is one other comment I would make, and it is this. I am not so sure that even if people do want to buy these existing houses, whether they should be encouraged by heavy debt to do so. I think one of the phenomena of post-war housing in Canada, in the price structure of post-war housing in Canada, is the manner in which the existing house has stood up price-wise as against the new house.

Undoubtedly depreciation has taken place, and certainly there is a tremendous amount of built-in obsolescence in the 1926 house. But notwithstanding this depreciation and the built-in obsolescence, the phenomenon is that we find these existing houses selling at about the same price per square foot as the new house, without the depreciation and without the built-in obsolescence, and the only offsetting factor being the extra value of the inside land. So I have some doubts ---

THE CHAIRMAN: Of the inside land?

MR. MANSUR: Yes; the inside land is worth more than the outside land.

THE CHAIRMAN: I see.

MR. MANSUR: I think it is a fair statement.

THE CHAIRMAN: That is, the location?

MR. MANSUR: Yes, Mr. Chairman. The factors that I mention being the phenomena must have as an offset the added value of the inside land.

THE CHAIRMAN: Those various categories that you have mentioned, taking the sale of the house in

the newer areas, of course that would not cause any difficulty. In the first place they generally talk of houses as built according to one standard plan, so that each one of them would maintain pretty well an equal value?

MR. MANSUR: Yes.

THE CHAIRMAN: And, of course, they are relatively new.

MR. MANSUR: Yes.

THE CHAIRMAN: And have not depreciated to any extent.

MR. MANSUR: No, Mr. Chairman.

THE CHAIRMAN: Naturally, you would expect them to be more marketable, and with the second group you would expect them to be less marketable.

MR. MANSUR: Yes.

THE CHAIRMAN: And, as you say, the third group, the value of the land is the only explanation of anything more than a nominal value.

MR. MANSUR: Maybe I did not make myself clear, Mr. Chairman. I feel that an F.H.A. type operation in area No. 1 would look after the problem. In area No. 2 ---

THE CHAIRMAN: Do we need it here? Is there a gap here in that class of house?

MR. MANSUR: I think it depends upon your degree of social consciousness.

THE CHAIRMAN: Has there been any difficulty in selling houses in that class?

MR. MANSUR: Oh, yes, tremendous difficulty.

I mean, every employee that moves has to find a buyer for his house.

THE CHAIRMAN: Yes, but there are agencies that bring parties together, and are there many houses that stand for a very long period without being sold, in that class?

MR. MANSUR: Yes, Mr. Chairman; there are, at the moment -- I hate to keep referring to Toronto; it sounds as if I am a Torontonian.

THE CHAIRMAN: You should be proud of that.

MR. MANSUR: In Toronto at the moment, the co-operative listings which are in the hands of these real estate people to whom you refer are some 22,000 in number, and they estimate that they handle about 50% of the take. So that as compared with the sale of new houses, which in Toronto this year will probably be of the order of 6,000 maybe, we have overhanging the market in Toronto houses of all kinds, probably something of the order of 40,000.

THE CHAIRMAN: Then are we not building too many houses in that area?

MR. MANSUR: No, I do not think so.

THE CHAIRMAN: If the houses are on the market, why encourage people to build new houses?

MR. MANSUR: I do not think we are building too many houses, Mr. Chairman, because this is a remarkable industry in that there is never any inventory in the house building field. In Canada the inventory -- I think I mention this in my brief -- is only 2½ weeks' supply. I can see, in spite of general views

held to the contrary, neither anything immoral or reprehensible about the house-building industry having an inventory. I do not know whey there should be the stigma which seems to be attached to a completed and unsold house.

THE CHAIRMAN: But your statement a few minutes ago dealt with houses for sale that have not found purchasers.

MR. MANSUR: Yes.

THE CHAIRMAN: And you intimated that there were quite a large number of houses.

MR. MANSUR: Yes, Mr. Chairman. But I think the criterion is not the number for sale; I think the criterion is the number that are empty. Before I would be particularly concerned about the volume of new housing I would want to see the number of houses that were empty in our communities.

We have some of them. Windsor is a bad place. But generally speaking the vacancy ratio is below any reasonable frictional vacancy ratio.

So that I do not think the fact that houses are for sale is any good reason to stop building the houses. I do not see the reason, any more than if there are a lot of shares for sale on the stock market.

THE CHAIRMAN: Yes, I see your point.

COMMISSIONER LEMAN: May I ask a question related to this, Mr. Mansur. You referred to the problems of areas 2 and 3. Are they indicative of what most conventional lenders have in mind when they

lend on real estate? Is it the property, so much the property that the mortgagor is not considered a very important factor in his own credit?

MR. MANSUR: Mr. Leman, the ways of the insitutional mortgage lender are strange. There is a tremendous amount of superstition and folklore connected with it. I have been in the business for a long time and I have never understood the superstition and folklore and I really cannot identify it. I cannot give you a satisfactory answer because I cannot see, for the life of me, why certain areas should be good and certain areas should not be good. I do not think in a long-term scale or pattern of residential real estate values it is possible for the over-priced 30-year house to maintain its level of value, and I would, if I were a lending institution, be very careful of the older house, not for the reasons they are, but rather because I think there is tremendous over-pricing in the older house sector. This may be their reason, maybe I under-estimate them.

COMMISSIONER LEMAN: Is there any reason to believe that because of this situation the average person who lives in that area is not as good a credit risk?

MR. MANSUR: I do not think there is any evidence. In fact, quite the contrary. Once again, if I may talk about Toronto, and then I will desist, the new Canadian groups, of course, are living essentially in the core or in the older areas.

I notice that when there are mortgages advertised for sale in the newspapers, the people advertising these mortgages never fail to say, "Chinese covenant," "Italian covenant," "Polish covenant," "German covenant" as a sales feature. So I would think that the general view about those covenants is very favourable, otherwise they would not be advertised as such. I suggest that the general covenant, ... in the core, is probably as good as anywhere else.

THE CHAIRMAN: Of course, a great many of those people believe in investing in real estate.

MR. MANSUR: Yes, Mr. Chairman.

THE CHAIRMAN: That is where they put their savings. For some reason or another, they think it is safe.

MR. MANSUR: Yes.

THE CHAIRMAN: And that values will gradually increase with the growth of the area around them.

MR. MANSUR: Yes, Mr. Chairman.

THE CHAIRMAN: And they generally, in the meantime, fill the house with boarders and gradually pay off the debt. That is the way they live.

MR. MANSUR: Yes, Mr. Chairman.

THE CHAIRMAN: It is very prevelant throughout that whole area today.

MR. MANSUR: With regard to gradually paying off the debt, I would like to suggest that they quickly pay off the debt. I looked at a block of about four million dollars of second mortgages made primarily to new Canadians, with five-year maturity. The actual average maturity

turned out to be three years and eight months. The debt is paid off with great rapidity, by reason of the multiple incomes within the kind of household that you referred to.

THE CHAIRMAN: And then they go and buy another house.

MR. MANSUR: Yes, Mr. Chairman. But they will not get stuck as badly on the second one as they did on the first one. The Canadians really gave these people quite a going over when they came into our cities.

COMMISSIONER GIBSON: The land in this area No. 3 to which you refer has in the past tended to become gradually more valuable. Have you any explanation of why this land of increasing value does not attract potential lenders? What you say about the people is true, as far as that is concerned; but you have this underlying factor of quite valuable land.

MR. MANSUR: You usually have an obsolete building -- as a rough rule of thumb, once again, in Toronto no institutional lender will look at a building if it lacks the primary facilities that lenders seem to think should be there. A bathroom is a good idea, and running water is a good idea too. They will not touch the house, generally again, unless it has a driveway or some facilities for an automobile, and in Toronto they will not touch the house unless it is solid brick. That, I cannot quite understand, because in Montreal there is no such thing as a solid

brick house, where the lenders lend quite freely. But this is one of the superstitions, customs or mores of the lending institutions. I cannot explain it to you; I just do not know what it is about.

COMMISSIONER GIBSON: You said, for example, that there were some new entries into the second mortgage area.

MR. MANSUR: Yes, sir.

COMMISSIONER GIBSON: Isn't this likely to attract other people?

MR. MANSUR: The term I used, "second mortgage", I used / too literally. The second mortgage sector looks after not only second mortgages in each one of these three areas I mentioned, but it also looks after the first mortgage in area No. 3. That is a generality and it can be contested, Mr. Gibson, as altogether too general a statement. But I think essentially it is true.

So that in area number one you find the lending institution in at a conventional rate in first mortgages up to the recent chaos in the interest rate structure at about 6 3/4 to 7, with emphasis on the 6 3/4.

Then, in area number two you find some of the lending institutions that specialize in older houses in making first mortgages, maybe not up to the full 66 2/3 per cent, but at an interest rate of about one per cent more than in area number one.

Moving into area number three, you move quite sharply into the second mortgage interest rate: 10% to 13% I would think, would be a first mortgage rate off Parliament Street in Toronto.

THE CHAIRMAN: Dealing with second mortgages, at the bottom of the page: "In the second mortgage fields effective interest rates are presently in the range of 12 to 15 per cent. "

MR. MANSUR: Yes.

THE CHAIRMAN: Of course, it would be difficult to assess just how that fits in with the total cost of the financing unless we knew how much that second mortgage was and how much the first mortgage was.

MR. MANSUR: Right.

THE CHAIRMAN: Then you would average it out to find out exactly what interest they are paying in the total amount; would that be a fair way of doing it?

MR. MANSUR: That would be a fair way of

doing it. In that connection I was really only referring to the second mortgage segment.

THE CHAIRMAN: Yes.

MR. MANSUR: If we got into area three where the second mortgage company made both the first and the second, I would not expect a rate of interest of 13½ per cent. So that, your point is well taken.

THE CHAIRMAN: But would you estimate what sort of interest rate you might expect?

MR. MANSUR: 9% to 10%.

THE CHAIRMAN: You would not consider that unreasonable under the circumstances?

MR. MANSUR: No. As a matter of fact, I don't think the present level of second mortgage interest rates is unreasonable at all. I marvel at how low they are having regard to interest rates charged in certain other sectors of our financial economy. I can think of a lot better risks that bear much higher interest rates than current interest rate on second mortgages.

THE CHAIRMAN: On the other hand, are those properties in those areas you are speaking of such bad risks where the land value is increasing with development?

MR. MANSUR: I don't think they are, but all I can do is report to you what seems to be the judgment of the market in such matters. I don't always agree with the judgment.

THE CHAIRMAN: Every once in a while you have an area of stagnation?

MR. MANSUR: Yes.

THE CHAIRMAN: And for a time in certain areas sales are very difficult to make. For various reasons people are not putting their money in there at the time. You have also mentioned that one of the usual methods of financing old houses is, in part, by giving a second mortgage back.

MR. MANSUR: Yes.

THE CHAIRMAN: And that puts a somewhat different complexion on the transaction compared with the case where you have a second mortgage separately arranged, which is generally expensive, and the interest rate is high?

MR. MANSUR: Yes.

THE CHAIRMAN: The second mortgage back may have quite a moderate interest rate depending upon the bargain between the two parties.

MR. MANSUR: Yes; in respect to second mortgages back in Calgary, Edmonton, Toronto -- and they are the only cities where I had a careful look -- I would think in 99 per cent of the cases the second mortgage arose in the vendor's hands as a balance of purchase price rather than the financing being arranged. Then, the vendor either sells that balance of purchase price or pledges it against a loan. There is quite a substantial change taking place from selling to pledging against a loan.

THE CHAIRMAN: You have on page 11 what you call a hypothetical case, which I found somewhat complicated.

MR. MANSUR: Well, I tried to put the simplest one in there, Mr. Chairman.

THE CHAIRMAN: What I wondered was, a vendor is about to buy another house in another city and is looking for $4,000.

MR. MANSUR: Yes.

THE CHAIRMAN: The vendor is a person who had a house worth $16,000 and an N.H.A. mortgage on it of $12,000, and without any second encumbrance?

MR. MANSUR: Yes.

THE CHAIRMAN: Why should he assume he should be entitled to get $4,000 as a down payment from a purchaser?

MR. MANSUR: My own view is that there is no entitlement at all.

THE CHAIRMAN: He seems to think he should get it because he needs it to buy another house somewhere else.

MR. MANSUR: I don't think he has any more entitlement to it than he has to a certain price for shares.

THE CHAIRMAN: If a purchaser comes along and offers $1,500 in cash and the vendor cannot get a better deal, he either takes it or leaves it?

MR. MANSUR: That is right.

THE CHAIRMAN: But the fact is he is able to dispose of that house on those terms.

MR. MANSUR: Yes, and the terms, Mr. Chairman, in the fringe areas, which is my area number one, are dictated very largely by the going down-payment

on new N.H.A. houses. The terms of the sale of existing houses changed very sharply in December 1960 when the terms of the N.H.A. changed.

THE CHAIRMAN: That was when it went from 90 to 95?

MR. MANSUR: Yes, the loan moved up so that the down-payment became about half what it was.

THE CHAIRMAN: What are your views on that move?

MR. MANSUR: Well, Mr. Chairman, I was a public servant for so long I now find myself faced with the enormity of making comment on government policy.

THE CHAIRMAN: You are still in the rut.

MR. MANSUR: Oh, a very bad rut. I can only say government does the darndest things for the darndest reasons. Why in the world they gave away the balance of all that was left in the way of down payment to stimulate demand at that time, I just can't understand. However, this was their judgment, and they run the country and I don't, and I guess we must accept it.

THE CHAIRMAN: For some reasnn they must have thought it was desirable to have more houses built at that time.

MR. MANSUR: Maybe. I didn't feel at that time that the effective demand had completely disappeared. However, this is a matter of judgment.

THE CHAIRMAN: Isn't a 5 per cent equity a pretty thin equity under any circumstances?

MR. MANSUR: Extremely thin.

THE CHAIRMAN: And a slight down-grading in prices could wipe it out very quickly, and more?

MR. MANSUR: Yes. In my opinion, I think one of the better things that we have done in this country in the post war years was the manner in which a long equity was kept in Housing Act loans. By "long" I mean 20 per cent which was the general pattern in the first ten post-war years, as against the Americans who, under the F.H.A., came down to 5 per cent very early, and then in the case of the V.A. came down to no down payment at all. I felt one of our assets was that we still had some room in which to stimulate effective demand.

COMMISSIONER BROWN: When you get down to 5 per cent, this just covers the real estate agent's commission on selling a house?

MR. MANSUR: Yes.

COMMISSIONER BROWN: So, the owner does not get anything out of it?

MR. MANSUR: No. I would think it is very much like an automobile you buy. There is 20 per cent depreciation when you drive it around the block. I am quite sure a house takes on a 5% depreciation the day after the first owner moves into it. But I think this is some more of the folklore. I don't think the margin of safety of mortgage loan can be measured by the amount of equity in the mortgage loan. Experience during the thirties showed this just was not the case at all. I happened to be with a mortgage company at

that time. We had thousands and thousands of good current accounts where there was a minus equity during the years 1930 to 1935.

COMMISSIONER BROWN: I was not suggesting the 5 per cent equity was a bad thing. I was suggesting this sort of a down payment, when somebody is trying to sell an existing house, makes it very difficult.

MR. MANSUR: Extremely difficult.

THE CHAIRMAN: What are your views as to the rental housing situation?

MR. MANSUR: I think we can take great encouragement in the manner in which rental housing is coming into English-speaking Canada. Rental housing in the province of Quebec is old and established. I was rather interested in a remark made here recently when they talked about Ontario being the most sophisticated province. Maybe in fifty years time they will catch the province of Quebec in matters relating to real estate. But I doubt it even at their present rather good rate of progress.

THE CHAIRMAN: You must have come from the west.

MR. MANSUR: In the province of Quebec we came out of war with a housing stock of 90 per cent rental and 10 per cent home ownership. The increments to the housing stock in the post-war has been about 30 per cent home ownership and 70 per cent rental. So, there is a slight swing in the province of Quebec towards home ownership. The swing has been entirely the other way in the English-speaking provinces.

... You may notice that in Toronto right at the moment rental housing is running ahead of individual housing by two to one. ... There is a pretty buoyant attitude towards the building of rental housing in our larger cities outside the province of Quebec. I am referring to Toronto particularly, but it is equally true of Hamilton, Winnipeg, other prairie cities and Vancouver. There have been very important increments to the rental stock. One might say it is not the right kind of increment, but, nevertheless, it is an increment. And I think there has been quite a change in the English-speaking wife towards living in multiple accommodation. I think the change is very healthy.

THE CHAIRMAN: Why do you say it is not the right kind?

MR. MANSUR: I think there has been a great deal of emphasis placed upon the apartment house. Although there is room for an ever-expanding stock of apartment house units, I think our greater need takes the form of row housing. I would dearly love to see in the English-speaking part of Canada the double duplex for four families, such as the pattern in the province of Quebec which, of course, is by far the most efficient form of housing which we have in the country. However, this is not yet particularly acceptable in English-speaking Canada. I can remember when the municipalities in English-speaking Canada would not let you build row housing. We have made a lot of progress, and the new maisonette development in English-speaking Canada is rental housing of a very desirable

family type. I think there is quite a change taking place, Mr. Chairman.

THE CHAIRMAN: While we are still on the subject of rental housing, perhaps you can deal with the question of lower income-type housing -- subsidized housing -- and express some views on that subject? We heard something about that this morning.

MR. MANSUR: Yes, I could hardly recognize it as the late Chairman of the Metropolitan Toronto Housing Authority. I believe the amount of subsidized housing will continue to inch up. We undoubtedly have a need in every one of our communities by families whose income is insufficient for them to enter the market place.

The thing I am not clear about is just what responsibility falls on whom for the looking after of these people. I have spent so much time in public housing that I find myself uncertain of even the fundamentals. The people who are certain on public housing matters are people who have never had anything to do with it. It seems to me there is a philosophical judgment to be taken about public housing depending upon one's degree of social consciousness. This is a very difficult premise upon which to base the need for public housing.

In the city of Toronto, where there are some 4,000 units of public housing, we have eligible applicants in the number of about 4,000. The turnover in public housing both here and in the United States is about 10 per cent per annum. I would think that our needs for public housing will for many, many years remain considerably greater than the willing-

ness of the municipality and the province and the federal government to satisfy those needs.

In the meantime, Mr. Chairman, I think there are some very favourable things happening in the rental housing field. The rather generous use by Central Mortgage of the limited dividend provisions has created housing somewhat under the economic rental: it works out to about $80 a month for two bedrooms, if I remember correctly, which is about $20 under the economic market.

That has filled a tremendous need, and there are about three or four thousand of these units in Toronto and this has done a great job and it has taken tremendous pressures off the housing authority for that band. Failing that assistance that band would be leaning on subsidized public housing.

There is one other thing that has happened in Toronto which is very fortunate -- and this is equally true in all other large communities -- and it is the enthusiasm of the apartment house builder, joined by the enthusiasm of the lending institutions, and this is causing great over-building in apartment houses and there are apartment houses which are now being built -- the new ones have no vacancy problems, they are rented like hotcakes as quickly as anything to people that come from two and one-half and three storey walk-ups, vintage 1945 to 1948, and there is where the vacancies are appearing, and I hope that it will not be too long before there is a very substantial break in the market on rentals in these older units. Already it is beginning to make itself felt, so we will then have what I think is quite a suitable spectrum, with the public housing at the bottom, the limited dividend next, the hand-me-downer apartment house next, and then the current supply on top. I think that we are making very real progress towards this.

THE CHAIRMAN: And also aside from that, you have the older houses in the central areas of the city which become accommodation of a similar kind;

sometimes they are rented, but generally I think they are probably well rented today?

MR. MANSUR: In the core of Toronto as at 1960 the free standing individual houses, other than apartment houses, showed 56 per cent home-ownership and 44 per cent rental.

THE CHAIRMAN: 56?

MR. MANSUR: Yes, 56 per cent home-ownership. By the "core" I mean Bloor to the lake and the Don to Bathurst.

THE CHAIRMAN: And in most of these places they keep roomers?

MR. MANSUR: Yes.

THE CHAIRMAN: And they help to pay for family expenses out of that additional income. That is the explanation of many of these?

MR. MANSUR: And there is a fair measure of multiple occupancy in that area. It is not as high as one would have expected; that was one of the surprises in looking at that core. I had expected to see a level of multiple occupancy three times the rest of Toronto and it only runs about one and and one-half times the rest of Toronto.

THE CHAIRMAN: I don't believe that there are any main points which I wish to cover in addition to these questions I have put to you. However, you do say that you are going right down to the basic problem of the desirability of home-ownership without sufficient financial resources?

MR. MANSUR: Yes.

THE CHAIRMAN: I think perhaps you have covered that already. I don't think I have any further questions.

COMMISSIONER BROWN: I would like to amplify this comment you make that you thought it too difficult to arrange some sort of financing along the lines of F.H.A. for this portion of the housing that came within the areas where conventional mortgages of 66-2/3 per cent were available now. Were you visualizing full insurance or some method whereby under N.H.A. it would be additional to bring it up to 80 per cent, and how practical would this be? Would this reduce some of the administrative costs of doing it directly on a full basis? In other words, if you made the condition the availability of the 66-2/3 per cent conventional mortgage, and then insured something above that?

MR. MANSUR: Mr. Chairman, my remarks about this not being a large problem in financing existing houses in area one, and whether lack of mortgages was decreased in the better part of area two, or all of area two, if you like, is, of course, subject to whether we can find a sufficient flow of mortgage funds to justify such a move. Now, you will recall ---

COMMISSIONER BROWN: You are answering my next question at the same time; that is fine.

MR. MANSUR: You will recall that this is not a new subject, this has been going on as long as I can remember, whether it would be desirable to adopt the F.H.A. technique to finance existing houses.

In my day, the two arguments against it were that if the financing of existing houses were made easier, then this would have a very great inflationary effect on the price of existing houses. This judgment, Mr. Chairman, was taken at the time when our multiple occupancy rate was over twice what it is now and when there just were not any houses for sale at all. Nevertheless it was taken at that time because it was felt that the price of the existing houses was just far too high.

The second reason was that the government of the day didn't like the idea, because we were struggling then as we are struggling now trying to find a sufficient flow of mortgage funds. Historically these are the two reasons and I suggest, Mr. Chairman, that these two reasons are just as pertinent today as they were ten years ago.

Now, I would put different emphasis on the inflationary aspects of the existing houses than I did then for the reasons which I mentioned earlier, but nevertheless I think that these are two good reasons for not doing it.

Now, there are reasons for doing it and this Commission has listened to reasons on and off for quite a while. Somebody must take a judgment as to whether this is a good idea having regard to what does it do to our flow of mortgage funds.

Answering your question more specifically, I don't think it matters much whether you insure the

top end or the whole of the mortgage.
In the N.H.A.at the moment everybody talks glibly about the whole loan being insured; the whole loan is insured, but if there is insurance on top 25 per cent I can hardly visualize a set of circumstances - unless we have a repeat of the mid 30's -- where the insurance on, say, the top quarter is very different to the insurance of the mortgage account as a whole, so that ---

COMMISSIONER BROWN: For instance, Elliot Lake?

MR.MANSUR: In the Elliot Lake issue were there reasonable selection used by the managers of the insurance fund, they wouldn't insure houses at Elliot Lake.

This is where the social implications start overlapping the financial implications.

In the States the F.H.A., I suggest, takes a strong line; it just will not be pushed around, they are running an insurance fund and they are not running a social agency and they stay very firm about it.

Since the Elliot Lake experience there have been certain other loans made in company towns.

I think I mention in my brief that sometimes there is a hiatus or a gap in this area until the company of the company town assumes some responsibility to give some guarantees on mortgages for housing.

Now, if that is done, then I suggest to

you that the insurance of the top 25 per cent is equivalent to the insurance of the whole. I admit your point, Mr. Brown, and the point has to be faced when any scheme is introduced, but I do think that the difference is more of form than of substance between the two.

COMMISSIONER BROWN: I was thinking also, would it simplify the administrative problems in having to have people go around and value houses, and so forth, if it were based on sombody else's evaluation and their willingness to loan the 66-2/3?

MR. MANSUR: Well, I can only answer you that I don't think that it makes any difference because if I had any responsibility for the fund and I was insuring the top 20 or top 25 per cent of it, I certainly would want to have a look at the risk before I started to put any insurance on, whether it was 100 per cent or 25 per cent because, as I mentioned earlier, in most cases I look upon the 25 per cent as being the same thing as the 100 per cent.

COMMISSIONER BROWN: One point about the F.H.A. practice. Do they insure loans on existing houses where no sale is involved?

MR. MANSUR: Yes.

COMMISSIONER BROWN: Thank you, that is all I have.

COMMISSIONER MACKINTOSH: Mr. Mansur, we perhaps now should go back to the beginning of your brief where you list a number of gaps or something which I think you called -- I forget what your term was,

but I think it was "areas of sluggishness", and the first one I got was this one you have been talking about, the isolated or company towns, and I took it from what you said that your view is that this is a problem that can be met, but can only be met if the company involved takes its reasonable share of the risk or takes extra risk.

Then you mention the gap in respect of new sub-standard or owner-labour houses, and you suggest, I think, that on the whole this has to be left to local resources and local solution. In what sense are these houses sub-standard? Are they sub-standard as financial risks or are they socially sub-standard?

MR. MANSUR: What I had in mind, Dr. Mackintosh, was that they were sub-standard as a structure and they might be sub-standard as to layout. I was thinking particularly of sub-standardness in relation to the physical qualities of the house including any land qualities that are there such as being smack up against a railroad track.

COMMISSIONER MACKINTOSH: Then the implication is that they are therefore sub-standard as financial risks?

MR. MANSUR: No, I don't think they are sub-standard as financial risks, Dr. Mackintosh, but I mentioned a bit earlier and it was mentioned this morning that the operations of Central Mortgage as a residual lender had pretty well removed the gaps that were existing provided that the

house meets their standards.

Now, if the house doesn't meet the standards of Central Mortgage, then this gap exists. The two main categories are those houses that do not meet the structural requirements and houses where equity is very hard to identify. These are the two main categories.

I think there is a remedial system, Dr. Mackintosh. I think we can find a method of doing it if it is felt that the gap was large enough and acute enough; I think there are ways of doing it, and a way was found in Nova Scotia to do it and there is no gap in this field in Nova Scotia.

COMMISSIONER MACKINTOSH: How did they do it there?

MR. MANSUR: The Nova Scotia government is rather more friendly disposed to co-operatives than certain other governments,

the Nova Scotia government has sponsored co-operatives for quite a number of years.

To over-simplify it, the arrangement was that the Nova Scotia government borrowed money from Central Mortgage and re-loaned the money to the co-operative and provided the supervision required in that co-operative, and although theoretically the standards of these houses -- the physical standards -- were up to N.H.A. requirements, I don't think that the Nova Scotia government would have their loan called if there happens to be less than 10 per cent glass area in one of the bedrooms. I would guess there

was just a bit of latitude in the standards in connection with that operation.

COMMISSIONER MacKEEN: You know that the government of Nova Scotia had to step in because the experience of the ordinary loaning companies was so unsatisfactory they didn't want to make any further loans to these bodies?

MR. MANSUR: Yes. There is the very great difficulty with standard mortgage practice where there is a high content of owner-labour.

COMMISSIONER MacKEEN: You mentioned that that has been the experience, there has been a falling out between the groups; they have become non-co-operative?

MR. MANSUR: But there were one or two projects in Halifax that were highly successful under this arrangement.

COMMISSIONER MacKEEN: A second-class house?

MR. MANSUR: Yes.

COMMISSIONER MacKEEN: Not the owner-labour.

COMMISSIONER MACKINTOSH: The credit unions have done something in this field, haven't they, in nearly all the provinces?

MR. MANSUR: Yes, the credit unions are in this field and, as I mentioned in my memorandum, the Caisse Populaire -- which is really in the same category -- really took this type of housing under their wing within their respective parishes. when I was in Central Mortgage we never used to hear much from the province of Quebec on this problem because it was so well looked after by the Caisse

Populaire. This is equally true on what other things in the housing field; we had less trouble in Quebec than the other provinces.

COMMISSIONER MACKINTOSH: Well, in this particular part of the brief you set out some historical periods and characterize our present phase as the one in which we have changed from a seller's to a buyer's market. Do you look on that as a long continuing phase, some place which we have arrived at and will likely continue in, or is it a preliminary to another phase, or do you believe that the teenagers will take us out of it shortly?

MR. MANSUR: No, of course that is nonsense; it is comforting, but nonsense just the same. I hesitate, with you of all people, to make any forecasts about the future.

COMMISSIONER MACKINTOSH: I am not pressing you to go further than you want to; I simply wanted to know how far you did go.

MR. MANSUR: I believe that the backlog of need resulting from both World War II and the depressed years of the thirties has been reasonably made good in absolute quantities, having regard to the cost-income relationship.

Now, if houses cost half what they do at the moment, then obviously the effective demand would be there in very large measure and I imagine we would be right back to where we were, say in the late forties. But having regard to the present cost-income relationship, I think that our housing supply has reached a relatively happy state of balance. By saying this, I do not mean that our housing situation is satisfactory for everybody, but I do think that the more pressing of the shortages have gone, and I think they have gone to a point that we have moved into a buyers' market; and, as I mentioned in my memorandum, I think that the tremendous rush of housing in 1958 may not have caused it, but it certainly showed that the change had taken place.

As to the future, I think that a revival of buoyancy in effective demand for housing depends very largely upon business conditions. After all, 99.5 per cent of all houses are sold to males who are employed. Now, in the first half of the fifties the increment to our male labour force was about at the rate of 75,000 a year. In the last five years it has been about at the rate of 25,000 a year. I think the housing market now shows some relief from the pressures of a substantial increase in the labour force

by those people who both can and wish to buy houses.

If economic circumstances change, become buoyant to an extent that we resume an annual increment of 75,000 males in our labour force per annum, then I think there will be a revival of the demand for housing. But I do not think, if we have a continuation of an increment of 25,000 a year, that we are going to see a very buoyant demand in the housing field until the change takes place.

Let me move on to the next question, this explosion of marriages that we are supposed to have about 1955 or 1956. They can explode and marry just about as fast as they like ---

THE CHAIRMAN: You mean, 1965 or 1966?

MR. MANSUR: Yes, 1965 or 1966. They can explode and marry as fast as they like. Unless the male member of this marriage has a job earning, in the Toronto area, something about $2.60 an hour, he is not going to buy a house. That is about the cut-off figure in Toronto. It would be lower elsewhere, but nevertheless, not much under $2 an hour anywhere else.

I have the feeling that much more important than the marriage rate is the employment of married men. For instance, to give you an extreme example, Dr. Mackintosh, in the year 1933 there were 65,000 marriages and there were 14,000 housing starts. Our post-war experience has been that the housing starts have run slightly over the marriage rate. We can have a situation where the marriage rate far

exceeds the amount of housing starts. Does that answer your question?

COMMISSIONER MACKINTOSH: Yes.

THE CHAIRMAN: We will adjourn for five minutes.

--- Recess.

COMMISSIONER MACKINTOSH: We will resume. The Chairman is unavoidably absent for a while. I would like to continue with another of the problems which your brief raises, Mr. Mansur, the fluctuating flow of mortgage funds from the institutional lenders in the N.H.A. and conventional fields. To what extent does this arise mainly or entirely from the fixed or spasmodically adjusted rate of N.H.A. lending, and to what extent does it arise from other factors?

MR. MANSUR: By "rate", do you mean interest rate Mr. Chairman?

COMMISSIONER MACKINTOSH: Yes, interest rate.

MR. MANSUR: Mr. Chairman, I think that perhaps the best example is to use the most recent one. In 1959 we had a bit of monetary chaos or a period of restraint in the monetary field, however it is best described, and lending stopped at that time. In December, 1960, the interest rate was moved to 6 3/4 per cent, at which time there were about 100 basic points difference between the five halves of seventy-five and the N.H.A. maximum rate. One hundred basic points is not sufficient to induce lenders into the

N.H.A.

This change in the N.H.A. rate in December, 1960, was accompanied by a fortuitous improvement in the bond market, so that about April or May, when the snow had gone, we had a spread of about 150 basic points between the five halves of seventy-five and the maximum rate of interest under the N.H.A. This spread, which was quite satisfactory, ranged up to almost 175 basic points immediately prior to the change in interest rate from 6 3/4 to 6½ per cent on November 7, 1961.

The reduced maximum interest rate under the N.H.A. still showed about 150 basic points difference, and the lending continued uninterrupted though the interest rate was changed.

We went on from there until about June, 1962 with the number of basic points ranging from 150 down to 130; I think it got down to about 120 without any great change in the rate of N.H.A.lending.

Then the circumstances of June, 1962, occurred when we got down to about 90 basic points, at which time all the lending institutions departed. The situation since then has been an improvement in the bond market, so that presently there are about 130 basic points showing as a differential. There is a kind of nosing around by some of the lending institutions who are not active in the market at the moment, perhaps anticipating that the bond market will improve. I suggest that they will be back in the market when 150, maybe 140 basic points show between five halves of seventy-five and the maximum

rate of interest. Does that answer the question?

COMMISSIONER MACKINTOSH: Yes.

COMMISSIONER MacKEEN: May I ask a question?

COMMISSIONER MACKINTOSH: Yes.

COMMISSIONER MacKEEN: Would you attribute that entirely to the spread between Dominion bonds and the C.M.H.C. rate, or would it in part be due to the fact that a lot of the lending institutions were, at least temporarily, tight on money themselves and were not investing in N.H.A. mortgages?

MR. MANSUR: No, I think it was entirely a differential in rates. The life companies seemed stuffed full of money. Immediately they left the N.H.A. sector for reasons of this too narrow spread there was a very marked upturn in conventional lending. I think it was entirely a matter of the N.H.A. rate being unattractive. I could see no evidence at all during this recent unpleasantness of the life companies being short of funds. This was not true of some of the other lending institutions, though.

COMMISSIONER MACKINTOSH: Is there a solution, or at least an accommodation to be found in either a fluctuating rate for N.H.A. or at least a more rapidly changing rate?

MR. MANSUR: Mr. Chairman, I think that in the evidence given -- I think, by Central Mortgage this morning, although it may not have been -- there seem to be three courses. One is the present one, of a very fixed rate, and the other is to enter into a system of discounts after the fashion of the N.H.A.,

and then there is the mid-course --

COMMISSIONER MACKINTOSH: You mean, F.H.A.

MR. MANSUR: F.H.A., I am sorry. Then there is the mid-course of trying to find ways and means of having the N.H.A. maximum rate reflect conditions rather more current than has been the experience to date.

I think a continuation of the present arrangements are quite unsatisfactory unless something could be done to keep government from forgetting all about this at most important times, and I despair of that.

The other extreme is the F.H.A. I suggest to you, Mr. Chairman, that the discounting of mortgages makes the maximum rate of interest as set by government absolutely meaningless, as indeed is the Congressional rate in the United States right at the moment. I mean, when you get all these Congress men sitting around and deliberating long and earnestly as to whether this rate should be 5¼ per cent, and in Seattle you see 5¼ per cent F.H.A. 203's selling at 93 to 95, you wonder what Congress spends so much time on it for. So I would hate to see the system of discounting introduced in Canada. I may say that the whole discount proposal was looked at very carefully by the government at the time the N.H.A. changes were made to the legislation in 1954. It was felt that the evils that accompanied the discount far outweighed the advantages of the discount, and that was not forgetting that there was the advantage

of the flexibility in the discount arrangement. But these things were weighed, and weighed very carefully with as good advice as could be found.

So that I feel a discount system is absolutely unthinkable until after some mid-course has been explored.

I think there are ways and means of finding a mid-course that would meet most of the need. It might not be perfect, but for goodness sakes, we are not looking for perfection as an alternative to what we have at the moment.

COMMISSIONER MACKINTOSH: This Commission has already given that up.

MR. MANSUR: I think there are ways and means of doing this; but, mind you, as I mention in my brief, it is much more comfortable for government not to be mucking around with changes in interest rates at any time; it is much more comfortable for them to sit under a discount arrangement, because they are at real arms' length and do not get into any trouble.

But I think the proper thing to do is for government or its agents to continue to control this rate with some sort of an arrangement which is considerably more flexible than the present one. I have some suggestions, but I rather hesitate to suggest government policy, or anything that might be suitable, because I think there is rather more chance of it coming into effect if I do not suggest it.

COMMISSIONER BROWN: Perhaps you should suggest things that you do not recommend.

MR. MANSUR: I think that would be a more reasonable course. However, at the risk of completely killing it by suggesting it myself --

COMMISSIONER MACKINTOSH: Then we will take it that this is the suggestion of one of your friends.

MR. MANSUR: Yes. I think one might look at a formula something like this. I think that the N.H.A. rate should be set every quarter, and I think that the progress advances which are made under N.H.A. loans should bear the interest at the rate for the quarter in which they are outstanding, and the changed rate for the next quarter would be applicable. I think that at the time of the sale of the house, the long-term mortgage rate should be the rate then current; and further, as the fourth step, the interest rate should be applicable for ten years, and that to the extent that these mortgages are existent ten years after the closing date, then they would bear interest after that ten years at the rate current at the end of the ten year period.

This is not all new. I realize that it sounds radical. My fourth point was exactly what was done under the old Dominion Housing Act. The rate was for only ten years.

COMMISSIONER MACKINTOSH: My information is not enough on this point. Does this contravene the principle that the borrower ought to be able to refinance after five years?

MR. MANSUR: No. I would think that amendments could be made in the Interest Act with good effect, but apart from that, just leave the

Interest Act as it is at the moment. The borrower has the right of repayment at the end of three years, with three months' bonus of interest, which at the present rates is something slightly in excess of 1½ points.

In the case of rental properties there is no right of repayment until the end of ten years. I would suggest that the terms might stay just as they are and that the interest rate on that mortgage should be subject to a recasting at the end of the tenth year in accordance with the interest rate then existing for new N.H.A. loans.

COMMISSIONER MACKINTOSH: But with a right of prepayment maintained?

MR. MANSUR: Oh, yes.

COMMISSIONER MACKINTOSH: I see.

MR. MANSUR: Yes.

COMMISSIONER MACKINTOSH: That is what I did not understand.

MR. MANSUR: Yes, Mr. Chairman. It is much in the way that home ownership becomes operative at the end of the third year.

COMMISSIONER MACKINTOSH: Yes.

MR. MANSUR: Mr. Chairman, I think that a great deal too much has been made of this short-term nature of the N.H.A. loan and the three years redeemable at 101½. This gets into bond parlance. After all, the holders of these mortgages have not just one little bit of paper in their hands about which they are frightened to death that somebody is going to pay off at the end of three years. most of the

lenders have thousands and thousands of these mortgages.

Really what we are talking about is not the right of repayment in full at the end of three years, although it would appear that that was what we were talking about, looking at / one instrument; what we are talking about is a certain flow of capital repayment in addition to the regular principal repayments to the regular amortization schedule.

I just feel there has been over-emphasis on this "one instrument" as against the thousands of instruments that are in the hands of the lenders.

COMMISSIONER MacKEEN: If there were a marked difference in the interest rates -- let us say, they fell by an appreciable degree -- the loans would be paid off and refinanced somewhere else. Certainly, we have had that experience in conventional mortgages.

MR. MANSUR: There seems to be a tremendous inertia among borrowers. I can remember being in the mortgage business in the late 30's where theoretically this should have happened to every loan in our portfolio because interest rates had reduced. With that company we spent a lot of time and energy trying to get borrowers to come into the office and sign a renewal agreement at a lower rate of interest. I don't think anything has yet been proven as to the manner in which refinancing will take place in a declining interest rate structure.

COMMISSIONER MacKEEN: Perhaps we are more susceptible in Nova Scotia.

MR. MANSUR: Refinancing has certain problems. The borrowers have got to go through the rigmarole of putting on a new mortgage, This is going to cost them, depending on how fortunate they are in the selection of lawyers, somewhere around one and a half per cent. It will cost them one and a half per cent bonus to get rid of the existing mortgages, so there is six months interest the owner is going to have to pay. Then I think it is probably the case that if the interest rate structure got too far out of line the lending institutions, themselves, would offer a reduced interest rate. This has happened before and

I think it will happen again.

COMMISSIONER LEMAN: But that risk of acceleration still makes an N.H.A. loan inappropriate on a retail basis for a small investor holding three or four?

MR. MANSUR: Oh, yes. I don't think one can reasonably anticipate any set of circumstances where these will be owned privately by individuals. I don't think they are a suitable instrument. Unless there are special circumstances, like a large estate, or even a small estate where the trust company arranges a take-out, I don't think we will see very much of this in the hands of the private individuals. They have had this arrangement in the United States for some time where FHA's can find their way into the hands of private individuals and it has never been very effective.

COMMISSIONER MACKINTOSH: In this area of the intermittent lender, the banks have had an important place, I suppose partly because of the ceiling interest rate for banks: would you think this was an important problem to solve? That is, the banks have an important function in this because of their branch system.

MR. MANSUR: Yes.

COMMISSIONER MACKINTOSH: And the only institutions that really cover the country.

MR. MANSUR: I am very enthusiastic about the banks coming in. As I mentioned in my brief, I think they have firstly the organization, the like of which we don't have in anything else in the country;

and the second thing is, I don't believe that the increments in savings should have the complete insulation thrown around them that they did prior to 1954, and which was re-accomplished in 1960.

COMMISSIONER MACKINTOSH: On the other hand, would you agree that even assuming the rate problem was wiped out that in a period of tight money the banks are likely to give priority to what you might call their working capital customers -- commercial credit?

MR. MANSUR: I think we have had a very good example of that in the various periods of monetary restraint. The banks withdraw, for reasons, I believe, other than interest rates, certainly with the 6¾ per cent interest rate established. I can hardly believe interest rate was one of their reasons for wishing to get out of the mortgage business. It was undoubtedly lack of funds that made them want to get out. As I understand the matter, the old legal opinion that was put forward by the bankers in 1954 was kind of dusted off and brought back into being. At this time the opinion happened to suit government, that this dusted off opinion should be applicable, which held that they could not operate under the Housing Act by reason of the Bank Act. This happened to suit government at the time for the wrong reasons, and the banks just departed. In my view I don't think there is any more reason for the banks to be out of the N.H.A. business today than there was when they went into it in 1954. But this is just my opinion.

COMMISSIONER MACKINTOSH: You mean because of their legal position?

MR. MANSUR: Yes, this legal opinion is the same reason why they said they would not come into it in 1954. The legal opinion was looked at by the law officers of the Crown and the law officers of the Crown said "nuts." About two days later the first bank came in and made twenty loans, and then all the other banks rushed in at a tremendous rate, and somewhere in the shuffle the legal opinion got lost.

COMMISSIONER BROWN: But this was all below the legal ceiling, wasn't it?

MR. MANSUR: Yes, but the point is that the Housing Act says, "... notwithstanding anything contained in any other statute, the banks may..." This point was just as valid at the time the banks came into the business in 1954 as it was at the time they departed, because one of the sections of the Bank Act says they cannot lend at over 6 per cent.

COMMISSIONER MACKINTOSH: In the absence of the Chairman I forebear to make any judgment on this.

MR. MANSUR: But, answering your question, I think it would be a great thing when the banks get back into this because I think it provides a coverage. I think it is a great tragedy that Central Mortgage and Housing has to look after all the outlying areas. I think we are building trouble for ourselves, and as soon as we get in a position where lending under

the National Housing Act emanates from the private sector, the better for everybody.

COMMISSIONER GIBSON: Leaving aside the legal question, you did say earlier there was a monetary problem.

MR. MANSUR: Yes.

COMMISSIONER GIBSON: And even if there had not been the legal question, there was still a monetary question: you agree with that?

MR. MANSUR: Oh, I agree completely that the banks did the right thing for the wrong reasons.

COMMISSIONER GIBSON: But you know what the problem is?

MR. MANSUR: Yes.

COMMISSIONER GIBSON: They only have so much money, and so many demands on them.

MR.MANSUR: Yes.

COMMISSIONER GIBSON: Have you any suggestion as to how to cope with that problem?

MR. MANSUR: No, Mr. Gibson. I have no quarrel whatsoever with the stand taken by the banks on account of the position they found themselves in at that time. I have no quarrel with that at all. I think they took the only steps that could be taken, but I would have been more satisfied in my mind, at least, if the real reasons had been given at the time rather than a dusted off 1954 opinion.

COMMISSIONER GIBSON: But I wasn't asking you so much if you thought they were right or wrong in any broad sense, but what you thought could be

done about the problem.

MR. MANSUR: No. I think, Mr. Gibson, that the capital pie is only so large. I would not go so far as to suggest that there should be a segregation of uses of notice deposits in the chartered banks. I don't think you can remake the system. I think if we were starting all over again we might have a little different set of circumstances, but I don't think you can unscramble the eggs. Nevertheless, I do feel the banks control a large part of personal savings -- I have absolute confidence in these banks doing the proper thing at times when they are able to do it, and the latter part of 1960 was not a time at which they should or could have made N.H.A. loans whether there was a Bank Act or not a Bank Act.

Over the course of the last few days, Mr. Chairman, I have rather gathered the impression from some of the representations made to you that housing, because it is so sacred, should not be subjected to any restraint. I think this is quite wrong. I think housing must be subjected to monetary restraint when all other sectors of our economy are being subjected to monetary restraint. However, that is a far different thing from saying that the most important sector of our personal savings should have this cloak of insulation around it against what I think is a very legitimate use for such long-term savings.

COMMISSIONER MACKINTOSH: But there are ups

and downs in monetary policy with some degree of intermittent participation of the banks in this field, quite regardless of the rate.

COMMISSIONER GIBSON: I would like to ask another question in the area you are raising, Dr. Mackintosh. You made clear that you didn't like the idea of N.H.A. mortgages being negotiated at discounts, Mr. Mansur.

MR. MANSUR: Yes.

COMMISSIONER GIBSON: I would very much appreciate it if you would elaborate that. I am not quite clear as to your reason on that.

MR. MANSUR: Well, I believe that one of the greatest accomplishments over recent years in the mortgage business is the elimination of regional interest rate differentials. I admit there are some small regional differentials still existing, such as in the Maritimes, but generally speaking these regional differences which were so pronounced prior to World War II have virtually disappeared, and I don't think this is only in the N.H.A. sector. I think this has been in a pretty broad sector. If the system of discounts was introduced, I have a feeling that we would re-introduce regional interest rate differences and we might find N.H.A. loans which were par in Toronto going for 94, 95 on Vancouver Island and maybe 96 or 97 in Nova Scotia, and I don't think this would be good. I realize you can make a case for it on pure economics, but I think there are some advantages to be gained in a country such as ours, that spreads

out the way it does and has the sharp regional distinctions anyway, to eliminate the regional distinction in matters of this kind.

The other thing that I believe is true in a case against discounts is that this gives the lender quite a leverage against the borrower, particularly in times of monetary restraint, and I just don't believe that even the lending institutions should have such a lever to be used against the builder -- and, in the final analysis, it is not against the builder at all ; it is against the home-owner.

My next point is this: there has been a tremendous to-do in the N.H.A. in order to keep the down-payments down to a reasonable level. As soon as you introduce a system of discounts, the whole discount goes on the down-payment, which I don't think is very desirable.

Then, my final point is that I question the propriety of a government-supported insurance fund providing the same insurance for a loan with effective yield, say, one per cent higher than other loans.

I think these are the reasons why I do not favour the introduction of the discount system, and I may say, Mr. Chairman -- and this may be improper -- the government spent a lot of time considering this very point at the time the 1954 amendments were introduced into the Act, and the very best advice that could be obtained by the

government at that time strongly suggested to them that even the inflexibility of a maximum interest rate was better than a system of discounts. I do not think, Mr. Chairman, there is any need to introduce a discount system to achieve enough flexibility in the interest rate pattern to serve the purposes that have been suggested before this Commission.

COMMISSIONER GIBSON: Could you have a free rate without a discount system?

MR. MANSUR: No. I think, Mr. Chairman, that gets over the down-payment problem, but I question the propriety under a National Housing Act of having different interest rates. I also think that it places an uncomfortable lever in the hands of the lender as against the borrower. The trouble is this, the lender is dealing in so many cases not with the eventual borrower. He is dealing with the middle-man in the form of a merchant builder, and as long as the merchant builder feels he can pass this on to the home-owner, then he is not too interested in what the interest rate is or what the discount is or anything else.

COMMISSIONER GIBSON: So you think it is an imperfect market, and that the borrower needs to be protected in this case?

MR. MANSUR: That is right, because the borrower, the man who is going to pay the freight for twenty years, is not in the picture at the time this transaction takes place.

COMMISSIONER MACKINTOSH: Any other questions?

COMMISSIONER GIBSON: Yes, I have some questions.

COMMISSIONER MACKINTOSH: I have finished with mine.

COMMISSIONER GIBSON: Going on to the portion in the memo under "Flow of Mortgage Funds" I would like to ask you a few questions running through this section of it.

You open up by saying that the housing sector has been the weakest borrower in the capital market and that it is supported by government, and the reasons which you give seem clear enough. I wonder if you would say a little more about how this developed? For instance, in about the 20's we managed to finance quite a lot of houses and the country wasn't as rich as it is now. Have our institutions changed? Have our ways of doing these things structurally changed so that there is a big gap here? You give us no background on this. You mention, for example, that there is a lack of local institutions in this business, comparing Canada with the States.

Now, my thought on the subject -- at least, I think it is true -- is that a great deal of this mortgage business in the 20's and before the First World War was done through local lawyers and other individuals in the local communities, and in these days this has dried up and this is one of the gaps which you are trying to fill?

MR. MANSUR: Let us go back a little further.

Let us go back to 1914 which is a good place to start from.

In 1914 the income earning investments of the wealthy farmer and the wealthy local man took the form of mortgages. I think I am correct in saying that a bond or debenture was unknown in Canada in 1914 save for the governmental transactions with the British government. Then, the first war came along and the first Victory Loans came in, starting I think in 1917

At that time there started an education of the Canadian people towards our ultimate role of being coupon clippers.

COMMISSIONER BROWN: Are you speaking for all of us?

MR. MANSUR: Those of us with any money. Then we come into the 20's, and although bonds were known they were a pretty restricted sort of thing. Mortgages and being the owner of real estate was still a pretty important sector, But the bond boys found out that they really had an instrument that could be sold. Marketability, the ease of transfer and all the other things that go with bonds and debentures started to come into their own. There is no question at all but that a bond or debenture is a more suitable instrument of investment than a mortgage. I think it was at that time that the swing started to take place from mortgages as being the popular form of investment, into bonds. I think historically, Mr. Gibson, this is the reason for it. I can't vouch for

it, but that is what I think. I just think that the bond boys came out with a better mousetrap.

COMMISSIONER GIBSON: In the later 20's there was the stock market, too.

MR. MANSUR: Yes.

COMMISSIONER GIBSON: In other words, new financial institutions of a competitive nature have grown up.

MR. MANSUR: Yes.

COMMISSIONER GIBSON: You talk in this same section about the optimum volume of new starts, and you talk about the years 1949, 1953 and 1959 as being exceptional years and you say that the optimum volume of new starts was limited by the lack of funds. You mean this simply in terms of what you normally regard as effective demand? These are years in which there were few funds?

MR.MANSUR: By "optimum" in that sense I mean a quantity sufficient to satisfy the effective demand, and I think in the final analysis that is the optimum of housing starts at all times.

COMMISSIONER GIBSON: Now, the burden of this whole discussion is that the intermittency of the supply of funds is [illegible] the central problem; that is correct, is it?

MR. MANSUR: Yes, that is correct.

COMMISSIONER GIBSON: What concerns you so much about the intermittency of the supply of funds? Is it that it raises the cost of housing, that it interrupts the flow; what are the main features

in your mind that makes this intermittency objectionable.

MR. MANSUR: Well, I think it is the impossibility of a merchant builder to get forward commitments to balance his activities ... That reflects into the cost of the end product for the home owner. I think it is very unhealthy for housing starts to go to 168,000 in one year and drop to, say, 115,000 the next. I just don't think that it lends itself to an efficient housebuilding industry and it seems to me that if there were a smoother curve ... it would be a lot better for everybody. I think that it adds costs to housing to have intermittency.

I remember on one occasion, Mr. Gibson, when the supply of mortgage funds was particularly tight and the builders had to restrict the production of houses to a much lower level than that to which their organization was geared; they were left with no other alternative but to put a rather larger price on the house if for no other reason than to meet their overhead. This is not good, and I think it would be bad if a motor car manufacturer, for reasons of this kind, had to cut his production away down and all his overhead had to go against half as many motor cars.

COMMISSIONER GIBSON: Isn't this a pretty competitive industry? Can people get away with that sort of thing for long? Can they still do that?

MR. MANSUR: No, I think the time that I refer to is the time when there was still a seller's

market; I think it is remarkable that the industry has changed so quickly to where the industry was able a year ago to absorb the whole sales tax imposed upon the Province of Ontario. Far from increasing the prices, they were reduced. I would not have believed that it would be possible.

Mr. Gibson, a lot of hard work was put into building an efficient house-building industry -- which was insufficient at the end of 1945. I think that the house-building industry is probably not as mature as other industries and I think for that reason it can stand some measure of protection in respect to the flow of mortgage funds. But to go back to the point which I made earlier, I don't suggest for a moment that there should be any insulation against periods of monetary restraint in respect to the house-building industry. I think such would be absolutely improper, and there have been traces of a suggestion along these lines to this Commission.

COMMISSIONER GIBSON: I am sorry, but I didn't get your last point; would you mind repeating it?

MR. MANSUR: My last point was that although I make this comment about the desirability of an evenness of flow of mortgage funds to get away from these periods of sluggishness, I just repeated what I said earlier that I don't believe that housing should be exempt from the effects of periods of monetary restraint.

COMMISSIONER MACKINTOSH: Go ahead, Mr. Gibson.

COMMISSIONER GIBSON: On page 17 you mention this point which has been discussed with Dr. Mackintosh, that there is nothing wrong in having a decent inventory of new houses?

MR. MANSUR: Yes.

COMMISSIONER GIBSON: And you say that the present supply is approximately 2½ weeks?

MR. MANSUR: Yes.

COMMISSIONER GIBSON: And you made the point, too, that if you have a fairly adequate stock in houses, that the benefits will have to filter to people who buy cheaper accommodation or rent cheaper accommodation. What would you regard as an adequate or a reasonable stock of houses; would a couple of months' supply be reasonable?

MR. MANSUR: Well, I am afraid that I must answer your question two ways. As one who has been interested in public housing in its social aspects ... I would like to see so many houses completed and unsold that it will force the price down by 15 per cent. But to the extent that I am presently engaged in trying to put together a mortgage account, and therefore have some concern about protection of that mortgage account, then I find myself enjoying this philosophy of the lending institutions who find that the stability of a mortgage account flourishes best in an economy of scarcity. Somewhere between these two points of view would be

the answer, but I can see nothing wrong with having a housing stock of completed and unsold houses of two or three months.

COMMISSIONER GIBSON: You don't think that that would affect the attitude of the lenders so much?

MR. MANSUR: It would drive the lenders crazy.

COMMISSIONER GIBSON: That would more than offset the benefits which you gain from it?

MR. MANSUR: It depends on whether you are thinking about this socially or financially; financially, I think the lenders would get pretty upset if they saw more than a month's supply. On the other hand, if I was only interested in the social aspects. housing welfare trade, I would like to see a six months' supply.

COMMISSIONER BROWN: How about the builders?

MR. MANSUR: I think that the builders would start to get uneasy if it was anything over a month's supply. I am just guessing on this, but this is my guess.

COMMISSIONER BROWN: If you had a six months' supply you would have the builders uneasy too?

MR. MANSUR: We would have quite a time ourselves.

COMMISSIONER GIBSON: But I am thinking of the future of the economy and in terms of

a reasonable flow of housing; there must be some point where you would get concerned even if you were interested only in the social side.

MR. MANSUR: I think about a month, maybe twice our present -- I think a month to six weeks; I think I would be concerned with anything over six weeks.

COMMISSIONER GIBSON: This takes me back to the question of intermittency, as one of the objections to the intermittent supply of mortgage funds, and that is that it may get the private lender fed up with this part of the mortgage market.

MR. MANSUR: Yes, I would say the private lenders may slip back toward the end of this year when there is a wide enough interest spread to entice them back into the market.

I just have the idea we may have some losses but most of the lenders will be back. In the meantime, no builder can plan his operations ahead. He does not know whether the lenders will be back or not.

You are speaking in the light of how does he know what to do about it; he does not know what to tell his sub-contractors and he does not know how to make plans under the present circumstances at all. I do not think it is very helpful.

COMMISSIONER MACKINTOSH: At the very simplest it is the unused resources?

COMMISSIONER GIBSON: Do you see any major changes in the structure of the building industry coming about, if we succeed in doing a major operation to prevent such intermittency?

MR. MANSUR: No, I do not think essentially that is the case. I think the house building industry has entered into a new period where conditions are much more competitive than we have seen in the post-

war years.

I think that these competitive conditions from which, incidentally, flow tremendous advantages, will be most competitive if the builders have reasonable assurance of funds and can do some preplanning. So that looking at the nature of the benefits that will flow through to the potential home owner I see tremendous advantage in having an evener flow of funds.

COMMISSIONER GIBSON: That leads to my last point. You have made it reasonably clear that you would like a more even flow of funds, and as a means of achieving this, the N.H.A. interest rate should be more in line with the market conditions. Are there any other elements in the terms of N.H.A. loans which you think would properly be varied to bring about this mortgage flow or, as was suggested this morning, have we used them all up?

MR. MANSUR: No, I think we move from there, Mr. Gibson, to the problem of where are we going to get the additional flow of funds. I cannot believe that anyone would be very satisfied to have government go on on an indefinite basis making good the deficiency in mortgage funds, between that which is required and that which is available. The very fact that government in the lender is an uncertainty in itselt in the flow of funds.

Therefore, in answer to your question I think we get right into where and how do we get a relatively even flow of funds.

In that respect the first problem is to find

the funds available and to remove the government to what I think is a more suitable position, that is purely a residual lender rather than an important factor in the mortgage market.

In my memorandum to the Commission I mentioned three or four possible sources of these funds. I believe that these sources of new funds and increased funds become more likely if steps are taken to make the N.H.A. mortgage and, indeed, the conventional mortgage, a more marketable instrument and one which is more competitive with other forms of investment instruments. For that reason I think a very good case can be made for a real effort toward the creation of marketability in the form of a secondary mortgage market.

I think this would do a great deal to increasing the supply of funds into the N.H.A. sector.

Really it does not matter whether funds come into the N.H.A. sector or the conventional sector, because they are two parts of the same thing. Whether they come into the conventional sector or the N.H.A. sector does not make me too excited, particularly in view of my suggestion that there might be additional sources of funds that will move more easily if we have the benefit of an improved instrument through a secondary marketing operation.

Now, Mr. Gibson, there has been suggestions made to this Commission -- I forget who it was that made them -- about the awkwardness of the instrument and unfavourable comparisons made with the F.H.A. instru-

ment. I do not think these remarks are justified. Certainly the views of the people in the United States are very favourably disposed to the N.H.A. instrument as compared to the F.H.A. instrument. I do not think there is anything basically wrong with the N.H.A. instrument, per se, other than that which is wrong with a mortgage in itself. Therefore, I think we are talking about an improved status of mortgages generally and not of N.H.A. mortgages particularly.

I can think of nothing that would improve the status of mortgages quite so fast as to have a secondary market in operation. I believe that mortgages are in an unfavourable competitive position to bonds and debentures. I think anything we can do to eliminate the kind of "me first" attitude of people interested in bonds and debentures would be a very good thing.

COMMISSIONER GIBSON: But your whole philosophy is one of trying to get a smoother flow and more sufficient supply?

MR. MANSUR: Yes.

COMMISSIONER GIBSON: I take it you do not see the housing policy as a major anti-cyclical device.

MR. MANSUR: I do not think that I would like to see housing in the box of tools for anti-cyclical exercises -- that is right.

COMMISSIONER GIBSON: It has tended to work that way in recent years?

MR. MANSUR: By chance.

COMMISSIONER GIBSON: Yes, but it has tended to go in that direction?

MR. MANSUR: There is no doubt about it. What evidence there is strongly suggests that that is the case. I think there are natural causes which make housing contra-cyclical, but the idea that this has taken place as though there was some wise man here sitting using housing in a contra-cyclical way has no basis at all. It just happened that way.

I remember, and I used to be with Central Mortgage and Housing, asking one of our regional supervisors: "What about housing next year?". He said: "I will tell you the amount of housing to the nearest thousand if you will tell me the amount of motor cars to be sold next year". You will notice that motor cars and housing are very counter-cyclical.

COMMISSIONER GIBSON: You told us about your ideas of how this might be varied, but surely you would be inclined to raise it a little less than other rates when times were good and reduce it a little less when times were bad with the anti-cyclical possibilities in mind? In other words, to be a little anti-inflationary when there is a boom and give a little encouragement when there is a recession? Is this one of the things you were thinking?

MR. MANSUR: You are really pinning me down now, Mr. Gibson. If I could be the one to lean against the wind, as you suggest, putting a little teeny weeny

bit here and a little teeny weeny bit there I would be in favour of it, but I am not so sure I would trust anybody else to deal in these little bits.

COMMISSIONER GIBSON: In other words you might want to have something a little closer to the formula basis?

MR. MANSUR: Incidentally, Mr. Gibson, there has been quite a lot of talk about that formula this morning, as if it was tied to the 20 year plus 2½ basis. There is no such time at all and there never has been. There needed to be some maximum.

Somebody put out some figures and thought that 2½ plus 20 years would be about right in latitude for the operators, but I gathered the impression this morning that there was a planned correlation.

I think that one of the great troubles in using housing as an instrument for counter-cyclical purposes, if you like, is that there is such a lag in housing. By this I mean anything you do today, really has no effect for nine months. I have never seen any judgment in Ottawa yet that gave me any confidence about what was going to happen nine months from now. So that I think that housing as a counter-cyclical measure is a very dangerous instrument to leave in anybodys hands.

COMMISSIONER MACKINTOSH: Would you say the same about public subsidizing of housing?

MR. MANSUR: Yes, I think so. If there were

some obvious vacuums to be filled and you could be reasonably sure of the lead time, I think it would be a proper idea to have public housing in such periods rather than periods in which all our resources were employed.

I do suggest, Mr. Mackintosh, going back to the point I made to Mr. Gibson, that we have not got too many people around who will take these steps, whether they be counter-cyclical or not.

COMMISSIONER MACKINTOSH: Is that primarily because the lead time is too long?

MR. MANSUR: The lead time is beyond the best guessers of those concerned with such matters, in my opinion.

COMMISSIONER MACKINTOSH: We have had the suggestion that the best way to be counter-cyclical is to be pro-cyclical.

MR. MANSUR: Well, I did not quite dare go that far, Mr. Mackintosh.

COMMISSIONER LEMAN: Mr. Mansur, I would like to ask you a couple of questions. Right after talking about the flow of mortgage funds, you go into another matter which is really much the same thing. You have the title: "Sources of More Mortgage Funds". We are talking about the same thing again. You say that there are two ways perhaps for the chartered banks to get back into N.H.A. mortgages, and if they interpret the law properly right now, or if the law were made a little clearer, what you mean is that the banks should be able to lend now at the

present N.H.A. mortgage rate, is that so?

MR. MANSUR: Well, I have not looked at the figures for two or three weeks, but had your question been asked two or three weeks earlier I would have had some doubt as to whether the chartered banks were in any position to do much lending.

COMMISSIONER LEMAN: I do not mean that.

MR. MANSUR: I am sorry.

COMMISSIONER LEMAN: I mean, they should be able legally to do it if they wished to do it. I am not talking about the availability of funds just now.

MR. MANSUR: Yes.

COMMISSIONER LEMAN: Then, presumably, you admit at page 18; you say, and you are talking about the pie not being of infinite size, that the answer to this is that there is no more important aim than increasing the housing stock. Without disputing that the fact is that,

it creates a shift in the use of funds. Don't you think a shift under the circumstances could go too far if we enable them to invest funds at 6 3/4 in respect of N.H.A. loans, unless they should be able to have higher interest rates on loans as well?

MR. MANSUR: Oh, yes. If you want my view on that, I think the sooner the limitation is taken out of that Act in respect of the rates the better for everybody. I think it creates very unnatural circumstances. There are too many strictures at this

time and the sooner we get rid of them the better.

I reserve from that statement the maximum rate of interest under N.H.A. loans because I think there are other reasons for that maximum rate of interest.

COMMISSIONER LEMAN: The second source you talk about is foreign funds.

MR. MANSUR: Yes.

COMMISSIONER LEMAN: There is something that puzzles me a little bit in the way you comment about this. First of all, you talk about the reported amount of the potential transactions usually in multiples of $100 million although occasionally fractional amounts of $100 million are reported. In what sense do you use the word "reported" there?

MR. MANSUR: Well, I am afraid I was trying to be facetious. You never hear of any of these American reports unless they are in multiples of $100 millions. A man says: "I have $200 million here, or $300 million to invest". They are always in multiples of $100 millions. Very seldom do you hear of the fractional amount of $50 million when you hear about foreign funds, and in very few instances do you see any folding money.

COMMISSIONER LEMAN: What I am trying to understand a little more clearly in respect of your comment is, are you talking about direct investment here?

MR. MANSUR: Yes.

COMMISSIONER LEMAN: So you make a difference

between what you call direct investment and indirect?

MR. MANSUR: Yes, I am talking direct investment, Mr. Leman, yes.

COMMISSIONER LEMAN: So it is possible that some loan companies in Canada could be using funds of United States, but you would not class that as direct investment in Canadian mortgages?

MR. MANSUR: No.

COMMISSIONER LEMAN: Would you think there is some of that money coming in now; that it has found its way into mortgages?

MR. MANSUR: Oh, yes, I think indirectly, Mr. Leman, that is quite true. For instance, I think to the extent that Metropolitan Toronto, or other municipalities are borrowing in New York, this provides relief to lenders in Canada, which in turn provides a leaway to mortgage lending. I think it is difficult to put these various borrowings into arithmetical perspective / although they are inter-related. Therefore there is a mortgage component in all New York borrowing that is going on at the moment, even that by the federal government.

COMMISSIONER LEMAN: You mentioned as an obstacle to this the uncertainty as to whether some people would be deemed to be doing business in Canada, if they were in this business.

MR. MANSUR: Yes.

COMMISSIONER LEMAN: Let us assume that it should be resolved somehow. Imagine upon foreclosure a lender would find himself renting premises, for

example, would that mean he was doing business in Canada?

MR. MANSUR: This is one of the fears and, of course, the withholding tax, Mr. Leman, makes it onerous for the mortgagee not only on investment income but even more when he gets into the position of an owner of foreclosed property, because, as I understand it, the withholding tax is not upon the net income but upon the gross rentals.

COMMISSIONER LEMAN: Perhaps that could be a matter of treaty?

MR. MANSUR: Yes, except, Mr. Leman, I believe the two other difficulties are much more important than that one. I think the exchange hedge is the really important one.

COMMISSIONER MACKINTOSH: Nobody is selling 20 year swaps.

MR. MANSUR: No, although I may say, Dr. Mackintosh, that I ran into a boy in Winnipeg who must have been all of the age of 25 years. He wanted some advice about attracting United States funds into the Winnipeg N.H.A. market. He needed my advice so he told me what he had done. All the boy had done was to find $1\frac{1}{4}$ million of Chicago funds which he passed as N.H.A. loans in the hands of his client builder and had arranged a 15-year forward hedge on a private basis to cover the interest payable to the American owners. He wanted my help because at one time I had one foot in the foreign exchange control board.

COMMISSIONER LEMAN: You do consider that this would be a good use of foreign funds to make for Canadians; that this would be a good area in which to seek and use foreign funds?

MR. MANSUR: If we could find foreign funds, yes. But I have some doubts as to whether there will be a flow of foreign funds for the reason I mentioned. But then I go back to the point I made to you earlier. Although one looks upon this as a possible source because there has been so much talk about it, perhaps it does not make too much difference whether the American buys the debentures of a large corporation sold in the United States or the bonds of a municipality. After all, the proceeds are part of the capital pie which we must divide partially for housing.

COMMMSSIONER LEMAN: I have heard some argument on this score. Some people here have inhibitions about letting foreigners get control of our industry, and at least if they invested in mortgages they would not come and live in our houses.

As to the foreign funds, later on you go on to discuss what are the conditions under which a good secondary market can be developed.

MR. MANSUR: Yes.

COMMISSIONER LEMAN: A good secondary market would help in this area too, would it not?

MR. MANSUR: Oh, very much, because you might be able, with a good secondary market, to arrange a take-out on some sort of terms.

COMMISSIONER LEMAN: One of the other important new sources you mention are pension funds which are growing and seem destined to grow a great deal more. There again, you say that the development of a good secondary mortgage market would help, would induce pension funds more?

MR. MANSUR: Yes.

COMMISSIONER LEMAN: But is it just lack of sophistication, or are there other obstacles now that explain why pension funds are not more investing in mortgages, N.H.A. or other kinds?

MR. MANSUR: Yes, I think there is a very good reason. In fact, I am rather depending upon it. I think that the knowledge of the treasurers of pension funds about mortgages in general, and N.H.A. mortgages in particular, is not as full as it should be. I think there is opportunity in this field, particularly, Mr. Leman, when you look at the report of the D.B.S. on pension funds as at the end of 1960 and see that the average interest earnings on pension funds for the year 1960 - the last reported figures - is almost exactly 4½ per cent, as compared with interest earnings of the life companies of 5.58 per cent in the same year. It seems there may be some opportunity for some rather higher interest-bearing investments.

COMMISSIONER LEMAN: And yet trust companies know a lot about mortgages, including N.H.A. mortgages, and trust companies do administer a lot of pension funds. Do you find that those administered by trust companies have a higher percentage of their investments

in mortgages?

MR. MANSUR: It is almost impossible to get those figures. The trust companies are not too anxious to hand out to people like myself just what funds they do operate and just what the asset distribution is.

There is one point. There is a misleading statement in that paragraph where I talk about 5 per cent of the investment of pension funds in mortgages, both N.H.A. and other. That 5 per cent has reference to the pension funds other than the pension funds of the Crown companies. The Crown companies have 25 per cent in mortgages; other pension funds have 5 per cent in mortgages, which averages about 8 per cent. The figure quoted to you yesterday is the correct figure. That 5 per cent is the non-Crown company sector.

COMMISSIONER LEMAN: Do you suggest there is better administration in Crown company pension funds?

MR. MANSUR: Oh, yes, I could accept that.

COMMISSIONER LEMAN: You do explain quite clearly in your brief, so I do not wish to go over all the remarks you make, about conditions precedent to having a good secondary mortgage market. But one thing I am still not quite sure of is whether you definitely feel that the conditions for having a good secondary mortgage market must take the form of good transferability of mortgages in themselves, or if there is more chance cost-wise of doing it through institutions which would issue their own debt securities,

secured or represented by blocks of mortgages, because there is the administration problem, is there not?

MR. MANSUR: Mr. Leman, it has already been mentioned to the Commission that there have been two or three of these companies set up with the general idea of debenturizing mortgages, usually mortgages purchased from Central Mortgage.

The companies which have been set up for that purpose have entered the market place to attempt to get their merchandise. The market place has imposed a price at a level at which there just is not enough margin as against long-term debenturization. The trust companies, with the benefit of borrowed money, which costs them rather less than long-term debenturization rates, are able to get by with it chiefly because the notice deposits in the trust companies tend to pull down their cost of money.

I cannot look into the future, but I will make the guess that unless the debenturization of mortgages by these companies takes the form very largely of short term debentures, there is not going to be enough room between the net yield on N.H.A. loans and the cost of their money to feed many mouths.

COMMISSIONER LEMAN: How about the whole spectrum of maturities?

MR. MANSUR: That is what I think they will be forced to do, the whole spectrum of them, but the

concept, I think, as I understood from you when you first introduced the subject, was kind of a matching in the long-term debenture. I think they must take advantage of the money markets - short and long - to make this thing add up and make sense.

COMMISSIONER LEMAN: You mean, a large portfolio of mortgages; that would make sense?

MR. MANSUR: Provided that there is enough leverage. Concerning leverage, representations were made to this Commission that 12½ times was not large enough; it should go to 15 times -- I do not think you need even 12½ times leverage to make money. But there must be some leverage and a big volume and a narrow margin, and dealings must be in wholesale lots. I do not think debentures can be sold to the public. I do not think you can debenturize N.H.A. to the public in small denominations. I think the cost of so doing in retail lots is too great.

COMMISSIONER LEMAN: In the development of the secondary market for mortgages as such, transferability of mortgages as instruments, you mention one obstacle that should be overcome, and that is the appraisal of mortgages. You say that would require a system of classification of mortgages?

MR. MANSUR: Yes.

COMMISSIONER LEMAN: Is that as simple as you make it sound here, the ability of a lender to appraise, say, a package of mortgages through this classification you suggest?

MR. MANSUR: Or his adviser would do it for

him. The classification of mortgages is taking place already. In one bid -- I guess it was auction number one by Central Mortgage -- the Calgary mortgages sold at something over 102.50 and the Vancouver Island mortgages were sold at almost par. Every one of the auctions has shown quite a wide range of classification. I cannot tell you what it is, because for some unknown reason Central Mortgage keeps this a dead, dark secret in their effects to develop a secondary market. But the only way you can judge classification is from transactions in which /that you have been successful or unsuccessful. If you want to know anything about the secondary market and its classification -- that everybody holds such high hopes for -- you must be a bidder on some of the packages, otherwise you cannot tell what happened. This is a gentle start of a secondary market.

COMMISSIONER MACKINTOSH: You would think there ought to be more market information?

MR. MANSUR: More? I think there ought to be the start of some market information. However, Mr. Chairman, I hasten to say, as one of the practitioners in this field, the more confused they keep it the better it suits me.

COMMISSIONER LEMAN: In your explanation of what you would consider a well developed secondary market you talk about these mortgage banks that should be in the market dealing all the time in mortgages. Do you really visualize a group of mortgage brokers and dealers, much as there are securities dealers?

MR. MANSUR: I visualize mortgage equivalents of Wood-Gundy and Dominion Securities and Ames, who stand in the market on the buying or selling side and have some access to some Central Mortgage bank. I hastened to add in that paragraph of my memorandum that these institutions do not have to be called banks, Mr. Gibson. They could be called something else.

COMMISSIONER GIBSON: What would you suggest?

MR. MANSUR: I think they should stand in the market on the buying and selling side, and that they should receive the same type of accommodation as the 14 bond dealers presently receive from the Bank of Canada.

I do not care whether this is through the Bank of Canada or Central Mortgage, or anyone else. But I also believe this thing can run without that accommodation by a central bank. It will not run as well, but I think this is a much better thing to try even without central facilities than to try to emulate Fannie Mae, for instance, or the Federal Home Bank System. I think those are perfect examples of things we should not do in this country.

COMMISSIONER LEMAN: But in the meantime you still see the administration of all these mortgages fairly concentrated in a restricted number of institutions?

MR. MANSUR: Yes, approved lenders, and approved lenders who have a national organization, because this is one of the problems. It takes a very large organization to buy mortgages on a national

basis, and there would have to be ways and means found for the servicing of these things,which will not be difficult to accomplish.

COMMISSIONER BROWN: I would just like to take up one of your remarks which you just made. What are these deficiencies of Fannie Mae that you talk about?

MR. MANSUR: The deficiencies of Fannie Mae are that it has elements of a central mortgage bank directed towards the development of various aspects of government policy. For instance, Fannie Mae has three main operations. There is the secondary market operation, which really consists in very wide swings of them either being a buyer or seller of mortgages, and if they are on the buying side they will stay there for 15 months; they will not sell. Then they become a seller, and become very reluctant to buy. They are an accommodation, however, to the mortgage bankers in the United States; really correspondents. If they get long Fannie Mae will buy them at some price.

The second operation of Fannie Mae is their special assistance, so that if the United States government decided there ought to be some military housing in Cape Canaveral, then Fannie Mae comes into the picture.

The third operation of Fannie Mae is what they call liquidation, which is nothing more than an agency for the United States government to liquidate the remaining assets of the R.F.C. mortgage corporation. Those are their three main operations. The statement

was made to this Commission the other day that the F.H.A. did not make mortgages in the same fashion as Central Mortgage . Technically, this is correct; the mortgages made are made for the F.H.A. by Fannie Mae in the form of purchases, and their operations are not far off, in order of relative magnitude, from the operations of Central Mortgage.

I do not think that Fannie Mae is geared to run the type of secondary mortgage operation that I visualize. I do not think that the secondary mortgage operation, either here or in the United States, should be run as primarily a governmental institution, any more than I believe that the Canada bond market should be run by the Bank of Canada as it relates to transactions with the public and institutional holders. I think if we are going to have a secondary market we must have people willing to stand in the market place whose relationship with the central bank ... is similar to the relationship of the approved list of 14 bond dealers.

I think Fannie Mae is thoroughly deficient for our purposes, but I do think that for these deficiencies, if there is a — thing ... about the selling of mortgages that we can learn from them, we should do so. For instance, if you go to Fannie Mae to buy mortgages there are posted prices and you say you are interested in 2 million on Long Island. They will bring you out a portfolio of 2 million on Long Island. They will give you the details and will show you the payment records and will also put a 15-day reservation against those mortgages

for you while you go out and have a look at them. With Fannie Mae you don't have to play, "Button, button; who's got the button", the way we now do in Canada.

But I do not think Fannie Mae itself, nor interested Americans believe that Fannie Mae constitutes a secondary market in the truest sense. The Federal Home Loan Bank System is really a central bank limited practically entirely to the conventional field for the benefit of the savings and loan associations. It is really a central bank operation and is not a secondary market per se.

COMMISSIONER BROWN: When they have posted prices, such as you have suggested, for a group on Long Island, do they have different rates for different parts of the country?

MR. MANSUR: Oh, yes. They differentiate the rate both on the buying side and the selling side.

COMMISSIONER BROWN: Do they establish this rate?

MR. MANSUR: No, they do not completely. The manner in which this is established is that Fannie Mae keeps closely in touch with the going market of mortgages under their system of discounts in various parts of the country. Today F.H.A. 5½ 203's are worth about par in Massachussetts, and are worth about 95 in Seattle. I would guess -- I am guessing at this one -- 93 in Pheonix, Arizona.

In the areas of lack of capital, ...--in the United States they have so many boundaries in the movement of capital, that fortunately we do not suffer

here -- there is a very wide variation. I would suggest that between New England, that has a surplus of capital, and the south west that has a deficiency of capital, that in today's market you might find six to seven points, and that is reflected in the posted prices of Fannie Mae.

COMMISSIONER BROWN: How would you visualize this happening in Canada, where there is no difference in the N.H.A. rates but there are differences in the bid prices on the tenders that have taken place?

MR. MANSUR: Well, we will have to have some practitioners in the market. The first should be Central Mortgage, if this is the way it is going to be done. They have had the experience of a number of bids; they know perfectly well that loans in Prince George will not bring as large a price as loans in Calgary. If we are going to have a secondary market, this is going to be some of the fun in it, to see whether the private practitioners are smarter than the people who are selling them.

COMMISSIONER BROWN: In this connection, in your brief you talk about the establishment of private mortgage banks, or whatever else you want to call them, and you refer to facilitating charters under the Loans Companies Act. Could you go into this in a little more detail, please?

MR. MANSUR: It seems to me that the most convenient vehicle for the mortgage banks -- which are not to be called banks -- to operate on is a

loan companies charter. Obviously such companies should have supervision.

They probably should have federal supervision. It seems to me that if a group wish to operate in the secondary market that there is lots of room for them to do so within the terms of a loan company charter under the federal Act. They are subject to certain necessary restrictions, but it is very clear as to the amount which they can leverage their capital. It provides a central source of information for all operations in this field, and generally I think it just so happens that we have a vehicle that fits the corporate structure of anybody who wants to be engaged in the secondary mortgage market. It is more by chance than anything else, Mr. Brown.

COMMISSIONER BROWN: Reference has been made to C.M.H.C.'s auctions.

MR. MANSUR: Yes.

COMMISSIONER BROWN: It has been suggested that in the development of a secondary mortgage market they might conduct auctions more frequently; not quite as frequently as treasury bills are auctioned, but at fairly regular periods; have you any comments on this?

MR. MANSUR: Yes, I think it is true. I think in all fairness, Central Mortgage and Housing were feeling their way [illegible] to start with. But I would think, if you are going to run a secondary market, there certainly should be auctions more often than once a quarter. I think if we could get over the abortive ones it would also be very helpful. I would suggest, perhaps for lack of a better figure, once a

month; I think that would about do the trick. I think the important thing is. If they want a secondary market they should let the practitioners know what is going on, rather than being kept as a state secret.

COMMISSIONER BROWN: They should publish a list of all the bids they get?

MR. MANSUR: Certainly. It is public business: why should not the public know about it?

COMMISSIONER BROWN: So, this would be another improvement you would recommend?

MR. MANSUR: Yes, I think there ought to be full information. After all, we listen to a lot of lip service in the House of Commons and elsewhere about the development of a secondary market. How in the world could you develop a secondary bond market if the Bank of Canada would not indicate their transactions, if the whole market in Canada was a deep, dark secret, and you had to guess on an average price of 98½ what the price was of the four quarters of 72 and the four halves of 83 and the five halves of 75, and treasury bills, and we just had to guess what the market was in each of those. This sounds ridiculous, Mr. Brown, but this is exactly what goes on in the marketing of mortgages.

COMMISSIONER BROWN: Have you any other suggestions, such as changing the size of the bundles?

MR. MANSUR: No, I think the bundles are all right. They come in $250,000 bundles, and in the giant economy size of $500,000. I think they are packaged all right. I can think of a lot

of things I would complain about long before the packaging.

Another thing I complain about is that you really have to be quite a detective when you bid one of these packages. You get about 47 or 48 loans in a half a million dollar package. There is absolutely no record of what the borrower looks like or his income. You are given the size of the loan. You are given the street -- not the street address, on which the house is located. It is pretty difficult if you get into Saskatoon and it is 33rd Street, and 33rd Street happens to be four miles long. You look at either end of the street for 2-year old houses because you know the loan was made in 1960. Then the list shows 1163 feet. Well, if you have been in the business you know that nobody but Mike Boychuk builds a house that has 1163 feet in it. So, you start reducing it to a house which is a Mike Boychuk type K. If you are lucky there is only one type K, but if there are four type K's you have to do a little more snooping. You can find out if you work hard enough. If you get a nice little crescent, as a street address, such as those in Regina, they are easy to find because there will only be one house of that type on the crescent. You know the number of feet, and the builders build that number of feet and you can find this house quite easily. However, this game of hide and seek -- fun though it is -- really doesn't seem to me to lend itself very much to rapid development of a secondary market. This is my main complaint, but from my point of view I repeat what I said to Dr.

Mackintosh, that from my own personal point of view I hope they do not change it.

Mr. Chairman, I wonder if I could say one thing?

COMMISSIONER MACKINTOSH: Surely.

MR. MANSUR: There have been a number of matters brought before the Commission some of which perhaps I could throw some light on. First, there is the matter of the insurance premium; there was some question on that. The present insurance premium, after you equate the different manners of collecting it -- and I think this was Commissioner Leman's question -- runs about 60 per cent of the corresponding F.H.A. premium.

The second thing I would like to say is that I missed one point -- and one of my colleagues reminded me of it -- in the discussion particularly with the Chairman: He asked me about the difficulties and the reasons for the attitude of the lending institutions about making loans in the older areas that I described as in area 3. I made some not too complimentary remarks about lending institutions on that occasion, and I withdraw them at this time for this reason: it was pointed to me that in the 30's, when there were heavy foreclosures, the incidence of foreclosure was much greater in the older properties than in the newer properties. There was the experience of the such heavy foreclosure to indicate that the older properties are more vulnerable.

There was a question asked during the course

of discussion, Mr. Chairman, about the volume of the second mortgage market. I can't remember which Commissioner asked that question. I think he was given the appropriate answer, that the volume is indeterminate. But as as a feel, and nothing more than a feel, I would guess that it probably is of the order of 200 million a year. I can't substantiate this. I just have a feel it is of that order as compared to the institutional and C.M.H.C. lending, N.H.A. and conventional, of about 1000 million.

A statement was made to the Commission there were no seconds behind N.H.A. firsts. I wish that were true. There are plenty of seconds around there. It may be an oil company second, reference to which was made in the brief from C.M.H.C. There may be a loan from Aunt Minnie; but, there are plenty of seconds.

Reference was made to the Commission to a letter from Dr. Weaver. Dr. Weaver said it was incomprehensible to him and his associates how anybody could go ahead with a programme of new housing unless there were N.H.A. in the existing house market. I can only say that when F.H.A. and V.A. between them get to a point that they cover as large a proportion of the new house market as does the N.H.A., then I will find the remarks from Dr. Weaver a little more convincing.

The term of the N.H.A. loans was mentioned, and this is a matter of judgment. There is no experience upon which to base judgment. We have had an increasing real estate market since about 1935. The war years intervened. We have had a general upward trend in interest rates. I suggest, Mr. Chairman, that any figures that were gathered in that 27-year period would be thoroughly suspect. However, for the guidance of the Commission I can say this. One of the two largest lenders in the United States considers an F.H.A. loan to be the equivalent of a loan amortized over a period of ten years. The other largest lender in the United States uses twelve years. The New York Savings Banks, the Dime and Bowery, who are very large lenders, use fifteen years. I think I agree with Mr. Bates. I have always been thinking in terms of fourteen years -- I suppose because it is not like one of these American numbers, and thirteen is an unlucky number, and eleven is too short. That is the rationalization of my 14 years.

I think, Mr. Chairman, those are all the supplementary remarks that I wished to make.

COMMISSIONER MACKINTOSH: Well, we are very grateful to you, Mr. Mansur. This has been illuminating to the Commission and extremely helpful, and we are particularly grateful for your frankness and concreteness in your answers.

MR. MANSUR: Thank you very much, sir.

COMMISSIONER MAKCINTOSH: We will adjourn

this hearing and the Commission will convene again on Friday morning at 8.45 A.M. when we hope to hear Professor Paul Samuelson.

--- Adjournment.

Supplementary Remarks by Mr. Mansur

In reading the transcript of my evidence before the Commission, I notice two inconsistencies upon which the Commission may wish to have my comment.

In the latter part of my submission I suggest that a secondary market might stimulate the flow of mortgage funds. It would be reasonable for the Commission to expect that my evidence on other matters would be consistent with my view that there should be a secondary mortgage market.

The first inconsistency is this. The Commission asked for my views about a change in technique to avoid the inflexibility of the maximum N.H.A. interest rate in relation to other interest rates. In my testimony I suggested:

(a) The maximum N.H.A. interest rate -- appropriate to other interest rates -- be set on regular quarter days.

(b) Interest payable by a builder on progress advances on houses for sale be at the interest rates current for the periods that these advances are outstanding.

(c) The N.H.A. interest rate -- for the home-owner and not for the owners of rental property -- would be reset at the end of ten years from the assumption date at the N.H.A. interest rate then current.

This suggestion is but one of a number of possible variations, the purpose of which is:

(a) To keep the N.H.A. interest rate more current with other interest rates.

(b) To relieve the house builder of the awkwardness of his having like houses for sale subject to N.H.A. mortgages at different interest rates.

(c) To lessen the "lending long" and the "borrowing short" difficulty of the trust and loan companies.

The advantages of this suggestion should be weighed against:

(a) The recasting of the N.H.A. interest rate at the end of ten years would cause some extra administrative work.

(b) Homeowners with N.H.A. loans would welcome a reduction and would dislike an increase in interest rate. On balance Government is likely to hear more about increases than decreases in interest rate.

(c) The lending institutions might not like the changed arrangements with the resulting effect of a lesser flow of N.H.A. mortgage funds.

(d) The inconsistency is that the present arrangement is better suited for N.H.A. originations to be traded in a secondary market.

The other inconsistency is this. I expressed the view that a variation in N.H.A. interest rates by region and community was undesirable and that real progress towards national mortgage interest rates had been made. During the testimony it was pointed out that for reasons of classification the price bid for N.H.A. loans being auctioned by Central Mortgage showed considerable variation in various parts of the country. The conflict is between the desirability of a national mortgage interest rate and a variation in interest rates by community to fit secondary market operations.

These comments in no way modify the testimony which I have given, but rather they bring to the attention of the Commission the advantages and disadvantages of various courses of action.

Royal Commission on Banking and Finance

CENTRAL MORTGAGE & HOUSING CORPORATION.

Hearings held at

OTTAWA

Vol.
43A

Date.
October 17, 1962



Official Reporters
F.J. Nethercut and R.J. Young
Toronto, Ont.

TRANSCRIPTION BY MEMBER
Nethercut & Young
Toronto, Ontario

SUBMISSION

BY

CENTRAL MORTGAGE AND HOUSING CORPORATION

TO THE

ROYAL COMMISSION

ON

BANKING AND FINANCE

SUMMARY

S. 1 Federal Government activity in the housing field on a continuous basis dates from the 1930's. Federal policy has been conducted under 5 main statutes:

The Dominion Housing Act, 1935.

The Home Improvement Loans Guarantee Act, 1937.

The National Housing Act, 1938.

The National Housing Act, 1944.

The National Housing Act, 1954.

S. 2 The Dominion Housing Act was designed to stimulate housing construction by increasing the supply of mortgage money available for this purpose and by increasing the demand for it. The supply of funds was increased by the direct infusion of Federal funds representing one quarter of the amount of mortgage loans made jointly with lending institutions, by interest rate subsidy to the private lenders, and by guarantees to these lenders against losses. The demand for funds was stimulated by the provision for high loan to value ratios, extended amortization, and limitation of the mortgage interest rate.

S. 3 The Home Improvement Loans Guarantee Act of 1937 provided for guarantees to banks and other lenders on loans made for the repair and improvement of residential property.

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The Dominion Housing Act was designed to stimulate housing construction by increasing the supply of mortgage money available for this purpose and by increasing the demand for it. The supply of funds was increased by the direct intervention of Parliament representing one quarter of the amount of mortgage loans made jointly with lending institutions, by interest rate subsidy to life insurance lenders, and by guarantees to these lenders against losses. The demand for funds was stimulated by the provision for high loan to value ratios, extended amortization, and limitation of mortgage interest rate.

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The National Housing Act, 1938, continued the joint loan technique provided for in the [illegible] Act and also provided for [illegible]

limited dividend companies, at long amortization periods and at low rates of interest, for the construction of rental accommodation for low income groups.

S. 5 The 1944 Act re-enacted provisions similar to those provided in the previous Acts. It contained an important new provision enabling the Federal Government to make grants to municipalities representing 50% of the [illegible] of acquiring and clearing slum property.

S. 6 The Central Mortgage and Housing Corporation Act, 1945, established the Corporation as the agency of the Federal Government primarily responsible for housing.

S. 7 Between 1944 and 1954 the 1944 Act was amended in two important ways. First the Corporation was empowered to use public funds for loans in cases where private loans were not forthcoming from private lenders as provided for in the Act. Second, amending legislation was enacted in 1949 which empowered the Federal Government, in partnership with provincial governments, to build and own housing projects with 75% of the capital costs and 75% of the operating revenues or losses being borne by the Federal Government.

S. 8 The National Housing Act, 1954, replaced the joint loan technique, whereby Government and private lenders had jointly made NHA loans on a 25%/75% basis, with a system of insured loans provided entirely by the private lenders.

periods and at low rates of interest for the construction of rental accommodation.

5.5 The 1968 Act re-enacted provisions similar to those provided in the previous Acts. It contained an important new provision enabling the Federal Government to make available multipurpose corporations for the purpose of acquiring and clearing blighted property.

5.6 The Federal Mortgage and Housing Corporation (FMHC) established the Corporation as the central agency of the Federal Government primarily responsible for housing.

5.7 Between 1944 and 1954 the FMHC lent its expertise in two important ways. First, the Corporation was empowered to use public funds for loans to those private lenders who were not fully covering the private lenders as mortgagees for 15 per cent of the second, amending legislation was enacted which empowered the Federal Government to [illegible] and own housing projects with 100% of the costs and 75% of the operating deficit borne by the Federal Government.

5.8 The National Housing Act, 1954, replaced the Joint Loan Committee, thereby Governments ordinate Agencies had [illegible] 25% basis, with [illegible] produced mainly by the [illegible]

The new Act admitted the chartered banks as approved lenders of insured mortgage loans. The new Act retained and continued the provisions of the earlier Acts insofar as they applied to public housing, slum clearance, limited dividend companies, and home improvement loans. It left largely unchanged the provisions enabling the Federal Government to engage in direct lending in cases where private loans were not forthcoming as provided for under the Act.

S. 9 While the 1954 Housing Act embodies a wide range of provisions, in actual performance its impact has been felt mainly through the mortgage market in the form of insured loans by private lenders and by the Government itself which undertook a greatly increased role as a mortgage lender in 1957 and later years. About 40% of all new housing starts in the period 1954-61 had some form of NHA assistance. Only about 2% however were assisted under those parts of the Act other than the insured loan provisions.

S. 10 The Act has tended to increase new house building in Canada by bringing forth a greater demand for mortgage funds and by increasing the total supply made available by Government and by private lenders. By providing more favourable borrowing terms for home owners than for rental entrepreneurs it has tended to increase the amount of home ownership building in relation to rental building.

S. 11 Life insurance companies provided about one-fifth

of the total of funds going into new residential construction over the period 1954-1961; banks provided one-tenth; trust and loan companies one-twelfth; the Federal Government one-seventh. Altogether these sources have provided just over half the total of funds used for new residential construction. They represented the principal source of financing however for about 75% of the dwelling starts over this period.

S. 12 About one quarter of the starts were financed entirely from other sources including the credit unions, which probably represented the main source of funds for about 5% of all starts. Individuals represent the largest remaining source of mortgage money and they represent also the main source of funds used to finance the equity in new residential construction.

S. 13 New residential construction competes with other uses for motgage money. Over the period 1954-61 about 38% of the total amount of motgage loans made was directed to new housing construction. Only a small portion of the remainder was for other kinds of new construction so that the bulk of it was secured by existing property, mainly residential property. As much of the existing property on which mortgage loans were made was already encumbered by mortgage debt, and as in most cases the new loans occasioned the retirement of the previous motgage encumbrance, the net amount of funds needed for the new loans is less

than implied by their gross amount. Thus on a net basis the claim on available mortgage funds made by new residential construction is greater than the 38% which represents its share of the gross amount of mortgage loans made.

S. 14 Mortgage lending represents one of the main uses of long-term capital funds. The net amount of mortgage lending in Canada over the period 1954-61, at 7-3/4 billion, was not much less than the combined increase in Federal, provincial and municipal bond debt, and was greater than the increase in debt represented by corporate bonds and stocks.

S. 15 Life insurance and loan and trust companies, in adjusting to capital market conditions, tended to reduce mortgage loan approvals in times of rising interest rates and increase them when interest rates were falling. This tendency was particularly pronounced in their NHA mortgage lending and reflected the comparative inflexibili of the NHA interest rate.

S. 16 The chartered banks, whose mortgage lending is confined to NHA loans, tended to follow a pattern of lending similar to that of the other private NHA lenders. The banks virtually stopped originating NHA loans at the end of 1959 as they were prevented by the Bank Act from originating such loans at more than 6% and because in the light of returns available on shorter term loans and other investments more liquid than NHA loans,

and cheaper to administer, new NHA loans had become unattractive.

S. 17 CMHC entered the mortgage lending field on a large scale basis at the end of 1957, primarily to stimulate employment. While the rate of lending by CMHC has varied since then, the Corporation has remained a lender of substantial proportions, partly because of the persistence of unemployment, particularly winter unemployment, even in periods of cyclical expansion, and partly also because of the withdrawal of the chartered banks as major suppliers of mortgage funds under the Act. Lending by the Corporation, while it has always been on a residual basis in the sense that CMHC only makes loans to applicants who have been refused private loans, has not consistently followed a pattern counter to that of the NHA lending of the private lenders. This is because the Corporation has not made residual loans to all classes of borrowers and has, in accordance with Government policy, varied from time to time the scope of its residual lending by changing the criteria of eligibility for loans.

S. 18 It would be inappropriate for CMHC, as an agency of the Federal Government, to make recommendations about mortgage lending measures or housing policy, except to the Government itself. Therefore, this brief contains no recommendations. Its final chapter however contains comment about a number of issues about which there has been considerable

public discussion in relation to Government policy. These questions include: the administered NHA interest rate; the application of the NHA exclusively to the new housing market; NHA mortgage lending by the banks, as it is affected by the 6% interest rate limit on bank loans; the legal constraints on the size of loans that may be offered by life insurance and loan and trust companies in their conventional mortgage lending; and the rudimentary state of the secondary market for mortgages.

CHAPTER 1

HISTORY AND PURPOSE OF HOUSING LEGISLATION

A. Housing Legislation

Housing Legislation in the 'Thirties'

1.1 The Government of Canada first entered the housing scene on a continuing basis when the Dominion Housing Act, 1935, was passed. Less than two years later, the Home Improvement Loans Guarantee Act, 1937, was passed and a year after that the National Housing Act, 1938 replacing and amending the 1935 Act, came into force.

1.2 While activity under the housing legislation of the 1930's was not on an impressive scale, the legislation itself has significance for establishing principles which to some degree have persisted since, although with important modifications.

1.3 The Dominion Housing Act, 1935, had the purpose of stimulating the construction of new houses, for housing reasons as such, and also for employment reasons. The stimulation of house building was to be effected through the mortgage nexus by the device of joint mortgage loans for the construction of residential accommodation. Mortgage loans were provided jointly by the Federal Government and private institutional mortgage lenders, mainly insurance companies, trust companies and loan companies. The Federal Government afforded loss protection to the private lenders depending on the amount of their participation in lending under the Act. The Federal share of the joint loan

provided at a low rate of interest. The private lender charged a higher rate and the borrower paid the resultant weighted average of the two rates. The size of loan in relation to the value of the property serving as security was higher than would otherwise have been possible for the private lending institutions to approve under the legislation governing their conventional lending activity. The loans were subject to a maximum interest rate, and were repayable by equal monthly instalments of principal and interest combined, over an amortization period of 20 years, which was long in the light of standard private lending practice at the time.

1.4 The joint loan technique had effects on both the demand for mortgage funds and their supply. It tended to increase the supply of funds by the direct infusion of the Federal loan share; by the provision of loss guarantees to the private lenders; and by the effect on the interest return to the private lender which was brought about by the provision of the Federal loan share at an interest rate below that charged to the borrower. The technique increased the demand for funds for new construction by affording mortgage loans which represented a comparatively high proportion of the cost of the real estate security and by extending the amortization period and thereby reducing the amount of income required to carry a loan of a given size.

1.5 The National Housing Act, 1938, confirmed the principle of joint lending contained in the

Act and introduced another type of specialized mortgage assistance which has continued to form a part of the array of Federal housing devices. The 1938 Act introduced the limited dividend company loan technique, whereby long term, low interest rate, high ratio loans were offered to help finance low rental projects for tenants in particular need. The companies qualifying for loans were to limit dividends on their equity in the projects so that the arrangement called for philanthropic or eleemosynary incentives from the initiators. The emphasis was on low rentals and low income tenants, and the initiative rested with private groups having authentic welfare motivations.

1.6 The Home Improvement Loans Guarantee Act, 1937, was intended to stimulate employment through the repair and modernization of existing dwellings. The Act authorized Federal guarantees against loss to private lenders making credit available for residential improvement. The technique has persisted in subsequent housing legislation.

The National Housing Act, 1944

1.7 The special conditions of wartime from 1939-1945 drew the Federal Government into housing measures relating to the allocation of space, the administration of rent controls and the provision of housing for employees of wartime industry, but these devices were not of continuing significance, and did not establish policy precedents which played a part in subsequent housing legislation.

1.0 The Home Improvement Loans Guarantee Act 1937

The acceleration of marriages during the war however, the increased pace of urbanisation, the rise in incomes, and the enforced limitation of new house building, combined to create a situation of congestion and housing shortage. The situation stimulated interest in housing questions and led to the passage of the National Housing Act, 1944, which was designed to help cope with the anticipated worsening of the housing shortage which would follow demobilization, and also to form an important part of the Federal measures to ward off mass unemployment which was widely regarded as an immediate postwar threat.

1.8 The National Housing Act, 1944, contained little that was new in principle, and rested mainly on three techniques which had been established before the war, namely joint loans, loans to limited dividend companies, and guarantees for home improvement loans. In subsequent years however, important amendments to the Act were made to meet particular pressures, as will be outlined briefly below.

1.9 The Act did contain a new provision however, to enable the Federal Government to assist in slum clearance projects. Under this provision the Federal Government was empowered to make grants to municipalities representing 50% of the costs of acquiring land in approved redevelopment areas, clearing the land, and preparing it for new uses, less 50% of the final value of the land so created.

1.8 The National Housing Act, 1954, contained [illegible]
tool was new in principle, and rumour widely on
three techniques which had been anticipated [illegible]
the war, namely joint loans, home [illegible]
dividend companies, and guarantees for home
improvement loans. In addition it [illegible]
important amendments to the [illegible]
mortgage powers, as well [illegible]

1.9 The Housing Corporation [illegible]
enable the National Investment [illegible]
National Savings [illegible]
to make funds [illegible]
of acquiring land [illegible]
clearing the land, and [illegible]

Central Mortgage and Housing Corporation Act, 1945

1.10 The Central Mortgage and Housing Corporation Act, 1945, established the Corporation as the agency of the Federal Government primarily responsible for housing. The Corporation has had the main task of administering the National Housing Act, 1944, but its activities have included the supervision of housing activities arising from other activities of the Federal Government which have involved housing or been clearly related to i

1.11 The Corporation was empowered, among other things, to buy and sell mortgages, or to lend on the security of mortgages. This power reflected a concept of the Federal Government as a potential source of funds which would enable holders of mortgages to liquidate or monetize them. The conditions under which it might be appropriate to do this were not spelled out in the legislation and in later years, when the Federal Government became a seller of mortgages in some quantity, the sales were carried out under other legislative authority. The concept, however, of a Federal Government role in a secondary mortgage market, or in the rediscounting of mortgages, was implicit in the Central Mortgage and Housing Corporation Act, of 1945.

Postwar Legislative Developments, up to 1954

1.12 During the postwar period and prior to the enact-ment of The National Housing Act, 1954, certain

important amendments were made to the 1944 Act.

1.13 There were a series of amendments which prepared the way for lending by the Federal Government directly, as distinct from lending jointly with the private lending institutions. In 1947 the Act was amended to enable the Corporation itself to make loans, corresponding in terms and conditions to joint loans, in places where private lenders did not provide facilities which would allow borrowers obtain joint loans. In some outlying areas and small towns the potential amount of mortgage activity was not sufficient to induce the private lenders to establish lending facilities, and in order that people living in such areas might not be deprived of the borrowing opportunities afforded by the Act, which were intended to be available to all Canadians, Parliament enacted legislation to empower the Corporation to make loans itself, without the participation of the private joint lenders.

1.14 In 1948 the Act was amended to provide a special kind of direct lending authority for the Corporation. In order to stimulate rental building the Government introduced a scheme whereby the risks of new rental investment were reduced through the provision of minimum rental income guarantees for approved projects. To serve as a further stimulus, lending institutions were authorized to make mortgage loans of up to 85% of the value of such projects, in place of the 60% that the legislation

governing such lenders would otherwise have allowed. Such loans were subject to an interest rate limitation below that which the lenders could obtain on joint rental loans or on conventional loans. In face of the possibility that the private lenders might not find lending on such rental gaurantee projects attractive, the legislation authorized CMHC itself to make the loans in approved cases where private loans were not forthcoming.

1.15 Another important legislative development in the first postwar decade was also related to deficiencies in the supply of private mortgage funds under the Act at the terms stipulated by the legislation. Joint loans under the original Act were subject to a maximum interest rate stipulated in the statute itself. In 1951, with the rise in the general level of interest rates, the 4 1/2% joint loan interest rate came to act as an impediment to participation by the approved lenders. The rate was raised to 5% in June of 1951 and the Act was amended to make the establishment of the rate a matter of statutory regulation. The statute itself imposed a limit on the rate which could be set by regulation, this limit being related to the current long term Federal Government borrowing rate. The rate was raised again in August of 1952.

1.16 During the period, 1944 to 1954, changes were also made in the statutory loan to value ratios that governed the size of joint loans, and in the maximum amortization periods allowed.

1.17 The regulations governing the maximum size of loan beyond which the statutory ratios did not apply were also changed as building and land costs rose.

1.18 In the mortgage field therefore, the Federal Government developed during the first postwar decade, a range of policy instruments, by which the pace of NHA lending could be affected. These instruments included the setting of interest rates, the fixing of loan sizes and amortization periods, and the determination of direct Federal lending policy.

1.19 In public housing policy there was one development of historic importance which merits mention even though it is not related directly to the mortgage market. During and after the war the Federal Government had provided directly a large number of Federally-owned public housing units for war workers initially and for veterans after the later stages of the war. This direct house building programme was terminated in 1949 but the Government was convinced of the need for a means of providing Federal assistance for the provision of public housing on a continuing basis. In December of 1949 legislation was enacted which empowered the Federal Government, in partnership with provincial governments to build and own housing projects, with 75% of the capital costs and 75% of the operating revenues or losses being shared by the Federal Government and 25% by the provincial government. The province under the legislation was free to

obtain any part of its share of costs from the municipality in which a project was to be located.

The National Housing Act, 1954

1.20 The National Housing Act, 1954, had the overriding purpose of increasing the supply of private mortgage funds for house building. It replaced the joint loan system, which had been in effect for nearly 20 years, with a system of insured loans for new house building. Apart from this it merely retained and continued the existing provisions of the National Housing Act insofar as they related to public housing, slum clearance, rental guarantee projects, home improvement loans, and loans to limited dividend companies. It also left largely unchanged the provisions empowering the Federal Government to engage in direct lending as distinct from joint lending under the previous Act.

1.21 The Act was designed primarily to admit the chartered banks and the Quebec Savings Banks as approved mortgage lenders under the Housing Act. Prior to this the Chartered Banks had been debarred from direct mortgage lending by the terms of the Bank Act.

1.22 Among the reasons offered to explain the exclusion of the chartered banks from the mortgage field was the illiquidity of mortgages and the short term nature of chartered bank liabilities. Without concession to the merits of this argument, it was believed that mortgage lending by the banks would be more acceptable if mortgages themselves were

more transferable, more easily marketable. And apart from the alleged particular requirement of the banks for marketable mortgages, liquidity of the mortgage instrument was recognized as desirable in itself.

1.23 To contribute to the liquidity of NHA mortgages, the Act provided for an insurance policy on each loan to protect the owner of the mortgage from loss in the event of default. The previous Act had afforded protection to the lenders against losses on defaulted mortgages. But the protection to the lender against loss under the joint loan system was in the form of accumulated credits to the particular lending institutions which originated the loans and it attached to these institutions as originators rather than as owners of loans. The loss protection was not specific to the individual mortgages themselves and was not inherently transferrable with the mortgages. The new system of insured loans incorporated the loss protection in an insurance policy specific to each particular mortgage.

1.24 The insurance of mortgages was conceived as an economic operation and was not provided without charge as was the case with the joint loan loss protection. The new Act provided that the insuranc was to be paid for by the borrower in the form of a single premium representing 2% of the mortgage amount in the case of loans on home ownership property and 2 1/2% in rental property. This

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1.24 The issuance of mortgage insurance

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represents the equivalent of about 1/4 of 1% in terms of annual yields over the life of the loan. The insurance premiums are accumulated in a mortgage reserve fund, out of which, insofar as possible, claims under the policy are to be honoured. Claims on the fund however, to the extent that they exceed the resources of the fund represent liabilities of the Corporation, and beyond that, the Crown.

1.25 The mortgage insurance now provides that in the event of default the owner of the mortgage has the option of retaining the property or making a claim under the insurance policy. The policy provides for cash payment in an amount representing the sum of 4 items:

a) 100% of the amount of mortgage principal outstanding;

b) the mortgage rate of interest for a period of default up to six months;

c) the mortgage rate of interest less 2 for a further period up to 12 months;

d) an acquisition fee of $150 and such taxable legal disbursements as may be approved by CMHC.

1.26 The insured loan is provided entirely by the private lender and does not involve joint participation by the Federal Government. The direct lending powers of the Corporation however, as they existed under the earlier Act were continued in the new Act in much the same form.

1.27 The new Act empowered the Corporation, in addition to the powers already contained in the Central Mortgage and Housing Corporation Act, to

sell insured mortgages, subject to the approval of funds by Parliament. The Corporation thus has powers to buy and sell mortgages under two separate statutory instruments.

1.28 In the new Act the loan ratios authorized were set above those prevailing under the '44 Act as amended, and the minimum amortization term to which the borrowers have entitlement was increased from 20 to 25 years. Maximum loan amounts beyond which the loan to value ratios in the statute do not apply were set by regulation at higher levels.

1.29 The interest rate continued to be fixed by regulation according to a formula depending on the long term Government borrowing rate. It was set initially at 5 1/2% which, as far as the borrower was concerned was 1/4% higher than had applied under the previous legislation. In addition the borrower was faced with the mortgage insurance fee which represented the equivalent of about 1/4% on the interest rate. On the other hand the 5 1/2% return to the lender was 1/4% lower than had been enjoyed immediately prior under the previous legislation. With the insured loan as distinct from the joint loan there is no difference between the rate paid by the borrower and the gross return to the private lender.

Legislation, 1954-1962

1.30 Since 1954 there have been two main new legislative developments under the Housing Act. The

Government, through CMHC has extended long term credit to municipalities for the development of sewage plant and trunk lines, and it has extended credit to Universities for the construction of dormitory accommodation. The legislation introducing these two new types of loan came into effect in late 1960.

1.31 Apart from these two items the Housing Act underwent little basic change in this period although authorized loan ratios and maxima were increased and the maximum allowable amortization period on insured loans was raised from 30 to 35 years (see Schedule 2, Appendix "A").

1.32 The principal developments in housing policy, as distinct from legislation during this period, were in the very greatly expanded role played by the Federal Government as a lender. The legislation itself remained basically intact.

1.33 Appendix A at the back of this report provides a chronological list of the main items of Federal Housing legislation, beginning in 1918 and leading up to the present.

B. Aims and Objectives of Housing Policy

1.34 The preamble to the National Housing Act, 1954, describes it as "An Act to Promote the Construction of new Houses, the Repair and Modernization of existing Houses, and the Improvement of Housing and Living Conditions". The general improvement of residential living conditions may be taken as

the proximate objective of Federal housing policy. But this in itself is so vague as to have little precise meaning, and it fails to account for objectives which housing policy in the past has often been used to pursue, and which are not directly related to housing as such.

Housing and General Economic Policy

1.35 Housing aims can not be followed independently of more general aims of economic policy, particularly employment policy. The entry of the Federal Government into the housing field on a continuing basis in the thirties was prompted by employment objectives as much as by housing objectives.

1.36 Housing, and particularly house building provided an almost ideal vehicle for Government to use in stimulating private investment and thereby creating employment. Housebuilding is pervasive; it is massive; it requires a comparatively high component of direct on site labour; it uses domestic materials for the most part; it has unusually large joint demand effects; and last but not least it is widely acceptable as a social objective and therefore as a basis for Government policy.

1.37 The National Housing Act of 1944, like the earlier Acts in the thirties, rested as much on general economic objectives as on housing objectives. While the exigencies of wartime greatly added to housing congestion, and while as a consequence there was a wide recognition of housing problems as such, and their likely exacerbation at the end

of the war, the '44 Act was designed not only to meet these problems, but also to contribute to the general level of investment and counteract the deficiencies in aggregate demand that were expected to follow the end of hostilities.

1.38 The Housing Acts of the 1930's therefore and the Act of 1944 reflected a duality of purposes, the stimulation of economic activity, and the improvement of housing conditions. The purposes were complementary, and not contradictory. Until the Korean crises in 1951 the stimulation of housing and general economic policies reinforced one another. In 1949 down payments under the Housing Act were materially reduced to stimulate demand and to counteract the business recession then being experienced. In 1951, however, with the rise in defence expenditures and the overall stimulation of aggregate demand thereby entailed, the first major use of housing policy as an anti-inflationary weapon took place and down payments were increased under the Act in February of 1951.

1.39 Higher down payments immediately reduced the demand for NHA loans but by the summer of the year even the reduced demand was more than the private lenders were ready to supply in the context of a higher general level of interest rates and the statutory maximum rate of interest under the Housing Act. The fixed NHA rate of interest in the early postwar period operated without leading to discontinuity in the supply of private funds as long as o[illegible]

of the war, the '49 Act was designed not only to meet these problems, but also to contribute to the general level of investment and counteract the deficiencies in aggregate demand that were expected to follow the end of hostilities.

The Housing Acts of the 1950's therefore and the Act of 1954 reflected a duality of purpose - the stimulation of economic activity, and the improvement of housing conditions. The former was a complementary, and not conflicting, policy. Until the Korean crisis in 1951 the stimulation of housing and general economic policies reinforced one another. To long down payments under the 1949 Act were materially reduced to stimulate demand and to counteract the business recession then being experienced. In 1954, however, with the re-emergence of demand threats, emphasis on the use of down payments as an anti-deflationary measure took place and down payments were increased under the Act in February of 1951.

Higher down payments immediately reduced the demand for NHA loans but by the summer of 1951 the demand was more than keeping pace with the supply. Lenders were ready to support the construction of a higher level or fixed rate loans and the NHA was

maximum term of interest rates and the [illegible]

rates of interest remained reasonably stable. During the 'fifties', however, the rate of house building under the Act was affected in the short run by the supply of private mortgage funds more than by any other single thing. Except for brief periods in the fifties there was a chronic excess demand for mortgage money at the borrowing terms available under the Housing Acts.

1.40 In the fall of 1957, Government made use of housing policy again to stimulate house building and to combat high general unemployment levels, and anticipated severe winter unemployment. In the context of excess demand for NHA funds the Government employed the direct lending powers available in the Act on a far wider scale than had been done in the past. Since that time, the Government itself has continued to act as a major lender, with modifications in its policy as time and circumstances indicate. The Government has never returned to the position of almost no direct lending that applied before 1957, but the degree of its commitment as a lender has been adjusted since 1957, largely in response to employment conditions. (See Chapter III).

1.41 From this brief and impressionistic account it will be appreciated that objectives having little to do with housing as such, have, from the beginning, played an important part in the formulation of housing policy. Housing policy, therefore cannot be understood in isolation, and represent one of the important instruments of the general economic policy of Government.

Housing Objectives

1.42 Housing objectives of course also play a part in the formulation of legislation and policy. But the housing objectives themselves are not specific or closely defined. The preamble to the 1954 Housing Act calls for the improvement of housing and living conditions. This statement implies that these conditions are not satisfactory. But neither the Act itself, nor any Government which has had the responsibility of administering the Act, has indicated what standard of housing conditions would be considered satisfactory. Improvement is called for, but no particular rate of improvement is specified and no definite terminal objective has been set. It is not possible therefore to designate a specific set of housing and living conditions as the objective of the National Housing Act, 1954.

1.43 Housing conditions could be improved either quantitatively, by an increase in the amount of residential space per person, or quantitatively by an improvement in the design or amenities or condition of the available space per person. It would be possible to improve housing conditions in one sense by improving quality even when the amount of space per person or per household was declining. Consumers, as users of dwelling space place a value on housing quality and for consumers in general there is some degree of improvement in the quality of housing that would more than compensate for a decline in the actual amount of space. In a market sense, consumers would

pay more for a given spatial amount of one kind of housing than they would for a greater spatial amount of some other kind of housing, provided that there was enough qualitative difference between the two kinds of housing. In the sense of this kind of market judgment then, the improvement of housing conditions enjoined by the Housing Act, could in certain circumstances be achieved when congestion in terms of the number of persons per room or per square foot or the amount of doubling up was actually increasing. This would be true only in a market sense, however, and it would reflect the behaviour of people purely as consumers and would be influenced by the distribution of income among them. Government policies are not judged by market criteria solely however, and they depend for acceptance on the support of the population, not purely as consumers, but as voters, and as judges of social objectives. It is difficult to believe that in this role, whatever may be their behaviour as consumers, many people would accept the view that housing conditions were improving unless the number of dwellings was increasing just as rapidly as the number of families and other households. Therefore an increase in the number of occupied dwellings in relation to the number of families and non-family households is apt to be regarded widely as one of the objectives of the National Housing Act.

1.44 Such an objective would indicate that the current new housing program should provide a number of new

units sufficient to look after the needs arising from the growth and movement of the Canadian population, and the loss of existing dwellings through abandonment, condemnation, accident, or demolition. It is difficult to forecast such demographic and economic events with confidence but in order to assign a rough order of magnitude to minimum housing requirements as defined by this particular objective, it is suggested that they would be in the neighborhood of 110,000 new units annually over the next decade, excluding needs arising from net immigration into the country.

1.45 An objective stated in terms of a minimum rate of housebuilding over the years is neutral as to technique. The National Housing Act provides for three basic kinds of assistance to new house building. There is the provision for the construction of public housing through Federal Provincial partnership. There is the provision for long term low interest rate loans to limited-dividend companies building rental accommodation for low income households. And there is the whole insured loan system aimed at assisting the provision of private housing for the general market with mortgage money provided by private lenders and by CMHC in certain situations when private funds are not forthcoming. While public housing and limited-dividend company housing have been important in achieving special results for low income groups, the loan insurance system has accounted for most

of the activity under the Act. Since the Housing Act of 1954 came into force there have been 414,500 new houses built under its provisions. These represent about 40% of the total of new starts in the period. Of these, 383,000 or 92%, were provided under the insured loan provisions. The dominant Federal Government influence on house building has been through the mortgage market.

CHAPTER 2

HOUSING DEMAND AS AFFECTED BY THE TERMS OF MORTGAGE BORROWING

2.1 The demand for housing of all kinds is affected by the terms on which mortgage money is available.

2.2 There are three main elements in the terms of mortgage borrowing: the amount of loan that can be obtained in relation to the capital value of the real estate serving as security for the loa the interest rate at which the loan is made; and the rate at which it is required to be repaid. An easing of the terms of mortgage borrowing means an increase in the maximum loan to value ratio or a reduction in the interest rate, or an increase in the repayment period or a combination of any two or three of these.

2.3 In a free and competitive market these mortgage lending terms would be established on the market, and they would depend on the demand of borrowers for loans of various sizes and maturities and interest rates and the supply of loans of various sizes, maturities and interest rates from the lenders. The relationship between mortgage interes rates, amortization periods and loan sizes would depend on the lenders' attitudes towards and assessment of yield,risk, and liquidity, and on the borrowers readiness to encumber future income in return for immediate cash.

2.4 To an important degree, mortgage lenders and borrowers in Canada do not have unrestricted rights

CHAPTER 2

to establish these mortgage lending terms on the market. In the first place the life insurance companies and the trust and loan companies, who represent the principal source of private institutional mortgage money are not allowed to make second mortgage loans at all under the legislation governing their activities, and in making conventional first mortgage loans are not permitted to encumber a property beyond two-thirds of its appraised value. The chartered banks are not allowed to make mortgage loans except under the National Housing Act, and under the National Housing Act, all approved lenders are subject to statutory and regulatory control of all three of the basic mortgage lending terms, interest rate, amortization period, and size of loan.

2.5 Thus in the NHA mortgage market, lenders are free to decide only the extent of their participation. In the conventional market, the banks may not participate and the life insurance and loan and trust companies are free to decide the extent of their lending and the amortization periods and the interest rates at which they will lend, but they are not free to vary the size of the loans they will offer beyond two-thirds of the value of the mortgaged property. Other private lenders in the conventional mortgage market are free to vary the amount of their lending and all of the terms on which they will lend.

Mortgage Lending Terms and the Demand of Home Owners

2.6 The demand of home owners for dwelling space in the form of owned houses increases as mortgage borrowing terms are improved. As far as mortgage interest rates are concerned the effect is obvious enough. A decline in the mortgage interest rate enables home owners, without any change in their down payment, to buy housing for a smaller amount of income over a given amortization period. Only those home owners with sufficient liquid assets to pay cash for houses, and with sufficiently low liquidity preference to hold a real estate equity representing the entire value of the house they own, would be unaffected in their demand for houses by a lower mortgage interest rate.

2.7 An increase in the size of loan to value ratio offered by lenders would also increase the demand for owner occupied houses. Such an increase would widen the opportunity for buyers to substitute income for cash in purchasing housing, and there are always potential buyers who would wish to do so. In an unrestricted market it might well be expected that excess demand for mortgage money would not exist in equilibrium, since lenders could in such a situation obtain higher interest rates. But the mortgage market, as has been explained, particularly under the National Housing Act, is not free and unrestricted and therefore excess demand for mortgage money at the available terms does exist.

2.8 Similarly the demand for owned houses can be

increased by an extension of amortization periods and the increased opportunity offered thereby for owners to substitute future income for present income in buying houses.

The Demand of Rental Entrepreneurs

2.9 The demand of rental entrepreneurs for investment in real estate is related of course to the rents they expect to receive and to the costs they have to incur. These costs are made up of equity and financial costs. The equity represents the immediate stake they must put up to acquire a property and the financial costs represent the stream of payments they must make to service the mortgage debt incurred in paying for the difference between the equity and the total capital cost of the project.

2.10 An improvement in the terms on which a rental entrepreneur borrows mortgage money could either increase his leverage or lower his borrowing costs, or extend his borrowing period which is equivalent to increasing his leverage over time. Any one or any combination of these would in itself enhance the demand of rental entrepreneurs for investment property and tend to stimulate the amount of rental building.

Owners and Rental Entrepreneurs Together

2.11 While a given improvement in first mortgage borrowing terms would increase the demand of those buying housing to own and those buying housing to let, the elasticity of these two demands would not necessarily be the same.

2.12 The impact on demand in the case of a reduced interest rate or an extended amortization period would arise from lower annual charges on the first mortgage. The degree of effect on demand would vary directly with the size of the first mortgage in relation to total capital costs. It would vary inversely with the cost of funds used in addition to first mortgage funds to finance investment in real estate. Generally speaking, rental entrepreneurs, as compared to home owners, are operating in a scale that affords them better access to funds that can be used in addition to or as a substitute for first mortgage money. Therefore, if rental entrepreneurs and home owners had similar first mortgage loan to value ratios, an improvement in mortgage borrowing terms in the form of extended amortization or reduced interest rates would have a greater effect on the demand of rental entrepreneurs than on home owners.

2.13 An improvement in mortgage borrowing terms in the form of higher first mortgage loan to value ratios would arise from widened opportunity to substitute first mortgage funds for funds from other sources in investing in real estate. The degree of its effect on demand would vary inversely with the first mortgage loan to value ratio itself and directly with the cost of obtaining funds other than first mortgage funds. Therefore if initial loan to value ratios were the same for owners and rental entrepreneurs, an increase in these ratios

would have greater effect on the demand of home owners than on the demand of rental entrepreneurs.

2.14 On the conventional mortgage market borrowing terms are available to home owners and to rental entrepreneurs on more or less equal terms. Institutional lenders are free to vary interest rate and amortization period but they may not go beyond 2/3 of value in loan to value ratio in first mortgage.

2.15 Under the National Housing Act the mortgage terms available to home owners and to rental entrepreneurs are the same with respect to interest rate and amortization period but they favour the home owner in some other aspects (see Schedules 2 and 3 to Appendix A). At present the home owner may obtain a loan representing 95% of the first $12,000.00 of value, and 70% of the remainder up to a maximum of $14,900.00. The rental entrepreneur is held to 85% of value up to a maximum of $8,750.00 per unit. A small difference arises also in the mortgage insurance fee which amounts to 2% of the loan for the home owner and 2½% for the rental entrepreneur.

2.16 The National Housing Act would appear to have stimulated home ownership building more than rental building. The Act permitted institutional lenders to offer higher first mortgage loan to value ratios than they could provide in the conventional mortgage market. This in itself, even if the loan to value ratios allowed in the

rental market were equal to those provided for in the home ownership market would have stimulated ownership lending more than rental lending. But the Act has accentuated this effect by the statutory provision for higher loan to value ratios for ownership housing than for rental housing, and by the regulatory establishment of higher absolute maximum loan limits for houses than for apartments. It is true that the Act also provided for amortization periods for both ownership and rental housing that were longer than the lending institutions were accustomed to observe on the conventional market, and that the demand of rental borrowers might be expected to be more responsive to changes in amortization periods than that of home owners. But the lending institutions were always free to offer long amortization periods. In this sense the provision for long amortization periods did not overcome any existing legal constraint in the mortgage market. Only in the provision for higher loan to value ratios did the Act permit the lending institutions to make a kind of mortgage loan that they previously were unable to offer.

The NHA and Mortgage Borrowers Terms

2.17 The National Housing Act has affected the demand for mortgage funds and for new housing in two ways.

2.18 First it has increased demand in total by the statutory creation of a mortgage market where borrowers can obtain higher ratio loans over long amortization periods. It has helped to compensate

for the added risk and illiquidity of such loans from the point of view of the lenders, by providing mortgage insurance. The interest rate under the Act has affected the supply of private funds made available for loans, but there has always been a substantial, if highly variable, flow of NHA funds from the private lenders. This indicates that at all times some lenders, and at many times many lenders, have preferred to do a sizeable NHA business rather than concentrate all their mortgage lending in the conventional sector. It suggests that the existence of the Act tended to bring forth a greater total supply of mortgage money, conventional and NHA together than would otherwise have been available, and a greater amount of residential building.

2.19 Second, the Act, by providing more favourable borrowing terms for home ownership than for rental, has tended to increase the amount of home ownership building in relation to rental building. Insured loans by private lenders under the Act during the period 1954 to 1961, have been approved for 317,000 new dwellings of which 79% were for owner occupancy. In the conventional mortgage lending sector, loans for 319,000 new dwellings were approved by the life insurance companies and the loan and trust companies during this same period, and 37% of these were for owner occupancy.

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CHAPTER 3

SOURCES OF FUNDS FOR NEW HOUSE BUILDING

3.1 Outlays on new housing in Canada from 1954-1961, roughly the period during which the 1954 Housing Act has been in force, amounted to $12.3 billion. The immediate sources of funds for these outlays were as follows:

(a) life insurance companies	$3,739 million	or 22%
(b) banks	$1,227 million	or 10%
(c) trust and loan companies	$ 956 million	or 8%
(d) government	$1,678 million	or 14%
(e) other sources	$5,745 million	or 46%

Life Insurance Companies

3.2 Life insurance companies have represented the main private institutional source of mortgage funds in the period 1954-1961. They have provided 22 percent of the new housing money over the past eight years. Their gross investments in mortgages on new housing have represented over 70 percent of their increase in liabilities in the 1954-1960 period and the increase in their total mortgage portfolio over this period has represented 62 percent of their increase in total assets.

3.3 The annual mortgage loan approvals of the life insurance companies during this period varied from a low of $378 million to a high of over $700 million. Their lending under the National Housing Act was particularly volatile, annual commitments being as low as $96 million in 1957 and $113 million in 1959, and as high as $282 million in 1954. The fluctuations

in life insurance company lending under the NHA are related to the statutory interest rate applicable and the ability of these lenders to make conventional loans as an alternative to NHA loans, the conventional loans being subject to no interest rate limit.

3.4 Life companies enjoy a particular stability in the sources of their funds, the flow of these being based largely on a historical accumulation of contractual obligations which are not likely to vary greatly over a short period.

Banks

3.5 Banks have provided 10 percent of new housing money since the 1954 Act came into force. While it is commonly believed that only a small fraction of the banks resources can be devoted to mortgage lending, their gross mortgage outlays in the 1954-1959 period, when they were actively engaged in mortgage lending, amounted to 55 percent of their increase in savings deposits and 26 percent of their increase in total liabilities. Their mortgage portfolio represented 6 percent of total assets at the end of 1961.

3.6 There have been wide variations in the annual volume of mortgage lending by the banks; their mortgage loan approvals in two years being over $300 million and in two others being less than $175 million. In the last three years, with the general rise in interest rates, banks have come up against the statutory limitation on loan interest rates contained in the Bank Act and this limit is too

low to encourage mortgage lending by the banks when the gross returns almost as high are available on shorter term loans. The banks have therefore virtually withdrawn from direct mortgage lending in the last three years.

Trust and Loan Companies

3.7 Trust and loan companies have provided 8 percent of the new housing money over the past eight years. They have been reasonably stable in their total mortgage lending but highly uncertain as lenders under the Act, their lending on insured loans ranging from $9 million to $175 million over the past eight years. Depending not only on deposits but also on short and medium term securities as their source of funds, they undergo substantial variations in the total flow of money available to them as their operations are sensitive to short-term changes in the structure of yields in the capital market.

3.8 Trust companies may well have an important role to play in the indirect placement of funds into the NHA market. As agents of primary investors who do not have direct access to NHA investment as approved lenders, the trust companies offer a means of acquiring NHA mortgages. In 1961 the trust companies made loans for over $15,000 new dwellings under the National Housing Act, and this represented about 3 times the volume of business they had done in any previous year. A substantial part of this lending undoubtedly

represented loans intended ultimately for investment by third parties. The banks for instance, while they do not originate NHA loans at more than 6%, may acquire such loans as investments at prices which promise to yield more than 6%. Pension funds may also wish to acquire such mortgages as high yielding investments. The trust companies, enjoying a necessarily close association with banks, and being in the position of administrators of a larger proportion of trusteed pension funds, would appear as logical originators of mortgage loans for these two secondary market outlets.

Government

3.9 The Federal Government has served as a major source of new housing money from late 1957 to the present for reasons originally dictated by general economic policy considerations and to sustain lending under the Act. Thus in the 1957-1961 period Central Mortgage and Housing Corporation disbursed $1.5 billion or 15 percent of the $8 billion expended on new housing. In terms of dwelling units, loans from Central Mortgage and Housing Corporation financed 131,000 out of the 663,000 units started. Thus one out of five dwelling units started in the 1957-1961 period was financed by direct government NHA funds.

3.10 Up until the fall of 1957, the Government had pretty well confined its direct lending, apart from loans to limited dividend companies for low rent projects, to home owner applicants in centres

of 55,000 population or less. In the face of the cyclical unemployment problem of 1957, and with the prospect of severe winter unemployment in the winter of 1957-1958, and in cognizance of a demand for mortgage loans at NHA terms far in excess of what the private lenders were prepared to meet, the Government altered its direct lending policy and made loans available to builders, rental entrepreneurs and also to home owner applicants in the larger urban cities. Builders were subject to a quota of 25 loans each. Dwellings built under the program were subject to a unit size limit of 1,050 square feet in order to avoid the use of public funds for luxury building. Rental projects were subject to ceilings on the prospective rent levels. All these CMHC loans were residual in the sense that borrowers had to provide evidence of their inability to obtain the loans from private approved lenders.

3.11 In the early fall of 1957 there remained about $150 million of an original appropriation of $250 million that was provided in the 1954 Act for this kind of lending. In less than three months this appropriation was fully committed, and in December a further $150 million was voted by Parliament. The demand for loans remained high and in February rental loans were suspended and have not been made available again. By April, 1958, the program came to a temporary end by virtue of the exhaustion of the $150 million appropriation

made available in November of 1957. A new vote of $350 million permitted the resumption of lending to home owner applicants and to those builders who had not used up the 25 unit quota allowed in the original arrangement. In the fall of 1958 a new quota of 25 units per builder was authorized, again to diminish the winter unemployment threat, but this time it was subject to a time limit and had to be acted upon by the end of the year, or forfeited. In 1959 loans from the first of the year were available only to home owner applicants until the fall when a new quota of 15 loans per builder was again authorized, this one also available only till the end of the year. Funds again ran out toward the end of the year and as Parliament was not sitting, the CMHC lending program was interrupted until March 1960 when an additional $500 million was voted. The program was then resumed on a different basis. Loans to home owners were provided subject to an income ceiling, which was applied in lieu of the dwelling size limit, in order to hold CMHC lending to a limit of $175 million for the year. The income ceiling, originally at $5,000 was raised in the summer and removed completely in October of 1960. While speculative loans to builders were not offered again, builders' loans were granted in the fall in respect of houses for which the sale arrangements had already been made. These non-speculative loans and loans directly to home owners have continued to be available since

the fall of 1960.

3.12 Direct lending since 1957 has thus been used as an instrument of government policy to stimulate house-building during periods of unemployment. Care was taken to ensure that this increase in housebuilding served the moderate income groups. When a scarcity of public funds developed, the financing of rental dwellings was abandoned and the amount of lending available to builders was carefully regulated to ensure that no large unsold inventory financed by public funds should accumulate. Finally it was necessary, in order to reduce Government's cash requirements, to limit even loans for home-ownership briefly during 1960, to the more moderate income groups. Since October, 1960, loans for home owner applicants, and non-speculative builders loans, have been available to all borrowers unable to obtain funds from the private lenders.

Other Sources of New Housing Funds

3.13 Table 3.c indicates that over the period 1954 to 1961, the lending institutions discussed above and Governments provided just over half, about 54%, of the funds used for new residential investment. These funds were spent on housing which is estimated to represent about 75% of the total value of new residential investment during the period, the difference being made up of funds used by the owners of the housing to supplement the first mortgages provided by the lending institutions discussed above and by the Federal Government.

3.14 Similarly, Table 3.f indicates that the life insurance companies, the trust and loan companies, the banks and governments represented the principal source of financing for about 75 percent of the total of new dwellings started over the period 1954 to 1961.

3.15 Of the remaining 25%, which represented 264,000 dwellings over the period, possibly as many as 50,000 or 60,000 were financed with the aid of first mortgage loans from credit unions. Credit unions as a whole in Canada had assets totalling about 1.3 billion at the end of 1960. The Credit Unions belonging to the Quebec Federation of Regional Unions of Caisses Populaires Desjardins account for about half the credit union assets in Canada. These Credit Unions over the five year period 1957 to 1961 made about 25,000 mortgage loans for new construction and for purposes other than business. The bulk of these loans were for new houses. The data suggests that mortgage loans for new houses on the part of all credit unions in Canada were in the order of 7,000 per year.

3.16 About one fifth of the new housing was financed without first mortgage loan assistance from the principal lending institutions, the Government, or from credit unions. Little is known in an organized way about the financing of this part of the housing program but most of the money came from the personal sector of the economy, fromindividuals, either in the form of mortgage loans or equity money.

3.17 The personal sector of the economy also provided most of the funds used to provide the down payment on housing for which first mortgage loans were made by Government, the lending institutions, and by credit unions. Loans in the form of second mortgages however, provided some part of the difference between total cost and first mortgage on this housing. Again little is known in an aggregative way about second mortgage lending. There is some recent information on second mortgage lending on housing financed under the National Housing Act. In 1961, of the purchasers of housing built by merchant builders with NHA loans, one in eight reported that a second mortgage loan was being obtained. This proportion varied by region: 25% in the Atlantic Region; 14% in Quebec; 13% in Ontario; 4% in the Prairies; 30% in British Columbia. These proportions represent understatements of the incidence of second mortgage lending, since a portion of such loans are not reported to the Corporation.

3.18 A sampling of the returns indicates that the terms on which the great bulk of these loans were made are surprisingly favourable to the borrower, when considered in the light of widely accepted folklor about second mortgage lending. The interest rate on these loans had a modal value of 6% in Winnipeg, lower than the NHA rate, 6-1/2% in Montreal, 6-3/4% in Halifax, and 7% in Toronto and Vancouver. The typical loan had an amortization period of 5

years in Winnipeg, 5 in Vancouver and Toronto, and 7 in Halifax and Montreal. Loan sizes ranged from $500 to $1,200 in most places although loans up to $2,000 were reported.

3.19 The explanation for the favourable terms lies in the source of the loans. Over 80% of them were provided by fuel companies, which indicates that the lender was concerned primarily with selling fuel rather than with the interest return on mortgage lending.

3.20 While fuel companies represent the dominant source of second mortgage lending on housing financed under the National Housing Act even in this sector they contribute probably less than 1% of the total investment in new housing.

3.21 Presumably second mortgages are more common in financing housing that is built with the aid of conventional first mortgage loans than they are in financing NHA housing. Higher equity requirements in the conventional market would tend to create a greater demand for supplementary funds. Presumably also, lenders like the fuel companies, who are in the mortgage business mainly as sellers of fuel, do not play as great a role in this sector of the market. In the NHA market, where down payments are comparatively small, a given amount of mortgage money can secure a larger market for fuel than it could in the conventionally financed market where higher average second mortgage loans would be required.

Table 3.a

Expenditures on New Housing by Source of Funds, 1954-1961.

($ Millions)

Item	1954	1955	1956	1957	1958	1959	1960	1961
Public Funds								
Public Housing								
Married Quarters for Armed Services	8.8	16.3	19.4	21.7	16.8	12.2	7.7	2.9
Federal-Provincial Housing, NHA	6.3	4.8	6.8	16.0	19.4	13.5	14.3	10.6
Other Public Housing	3.4	4.6	4.6	2.3	4.9	6.0	6.6	7.8
Loans Made by CMHC								
Limited-Dividend Loans	12.9	12.4	9.9	16.0	30.1	45.0	26.8	27.4
Other CMHC Loans	73.4	10.9	6.4	43.8	304.4	264.1	244.5	247.8
Other Government Loans	8.5	9.9	8.9	8.8	8.5	8.0	7.9	3.8
All Public Funds	113.3	58.9	56.0	108.6	384.1	348.8	307.8	300.3
Institutional Funds								
NHA Joint and Insured Mortgage Loans								
Chartered Banks	75.1	234.2	236.8	145.1	258.7	234.7	42.3	0.5
Life Insurance Companies	223.4	253.7	237.8	122.4	128.8	137.3	112.0	226.9
Loans, Trust Cos., etc.	13.4	34.3	42.3	9.2	35.2	27.9	23.1	160.3
Conventional Mortgage Loans								
Life Insurance Companies	66.8	120.5	166.5	183.6	158.7	228.2	200.8	171.4
Loan and Trust Companies, etc.	44.5	63.0	67.0	64.5	101.9	97.0	93.4	78.9
All Institutional Funds	423.2	705.7	750.4	524.8	683.3	725.1	471.6	638.0
Other Funds								
Equities of Owners in Addition to Above Mortgages	266.1	288.6	314.7	209.3	261.3	371.5	260.0	231.9
Other Financing	412.9	504.1	427.6	605.0	496.4	348.9	432.3	314.8
All Other Funds	679.0	792.7	742.3	814.3	757.7	720.4	692.3	546.7
Total	1215.5	1557.3	1548.7	1447.7	1825.1	1794.3	1471.7	1485.0

Source: Data for years 1959-1961 are from CMHC's "Canadian Housing Statistics" 1961, Table 34.
Data for 1958 are from "ibid" 4th Quarter 1960, Table 31.
Data for 1957 are from "ibid" 4th Quarter 1959, Table 31.
Data for 1956 are from "ibid" 1st Quarter 1959, Table 31.
Data for 1954-1955 are from "ibid" 1st Quarter 1957, Tables 39 and 40, and 1st Quarter 1956, Table 38.

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Table 3.b

Percentage Distribution of Expenditures on New Housing by Source of Funds, 1954-1961

Item	1954	1955	1956	1957	1958	1959	1960	1961
Public Funds								
Public Housing								
Married Quarters for Armed Services	0.7	1.0	1.3	1.6	0.9	0.7	0.5	0.2
Federal-Provincial Housing, NHA	0.5	0.3	0.4	1.1	1.1	0.8	1.0	0.7
Other Public Housing	0.3	0.3	0.3	0.1	0.3	0.3	0.4	0.5
Loans Made by CMHC								
Limited-Dividend Loans	1.1	0.8	0.6	1.1	1.6	2.5	1.8	1.8
Other CMHC Loans	6.0	0.7	0.4	3.0	16.7	14.7	16.7	16.7
Other Government Loans	0.7	0.6	0.6	0.6	0.4	0.4	0.5	0.3
All Public Funds	9.3	3.7	3.6	7.5	21.0	19.4	20.9	20.2
Institutional Funds								
NHA Joint and Insured Mortgage Loans								
Chartered Banks	6.2	15.0	15.3	10.0	14.2	13.1	2.9	0.1
Life Insurance Companies	18.3	16.3	15.4	8.5	7.1	7.7	7.6	15.3
Loan, Trust Cos., etc.	1.1	2.2	2.7	0.6	1.9	1.6	1.6	10.8
Conventional Mortgage Loans								
Life Insurance Companies	5.5	7.7	10.8	12.7	8.7	12.7	13.6	11.5
Loan and Trust Companies, etc.	3.7	4.1	4.3	4.5	5.6	5.4	6.3	5.3
All Institutional Funds	34.8	45.3	48.5	36.3	37.5	40.5	32.0	43.0
Other Funds								
Equities of Owners in Addition to Above Mortgages	21.9	18.5	20.3	14.4	14.3	20.7	17.7	15.6
Other Financing	34.0	32.5	27.6	41.8	27.2	19.4	29.4	21.2
All Other Funds	55.9	51.0	47.9	56.2	41.5	40.1	47.1	36.8
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Same as Table 3.a.

Table 3.c

Expenditures on New Housing by Source of Funds,

1954-1961.

Item	$ Millions	%
Public Funds		
Public Housing		
Married Quarters for Armed Services	105.8	.9
Federal-Provincial Housing, NHA	91.7	.7
Other Public Housing	40.2	.3
Loans Made by CMHC		
Limited-Dividend Loans	180.5	1.5
Other CMHC Loans	1195.3	9.7
Other Government Loans	64.3	.5
All Public Funds	1677.8	13.6
Institutional Funds		
NHA Joint and Insured Mortgage Loans		
Chartered Banks	1227.4	9.9
Life Insurance Companies	1442.3	11.8
Loan and Trust Cos., etc.	345.7	2.8
Conventional Mortgage Loans		
Life Insurance Cos.	1296.5	10.5
Loan and Trust Cos., etc.	610.2	4.9
All Institutional Funds	4922.1	39.9
Other Funds		
Equities of Owners in Addition to Above Mortgages	2203.4	17.8
Other Financing	3542.0	28.7
All Other Funds	5745.4	46.5
TOTAL	12345.3	100.0

Source: Calculated from the data in Table 3.a.

Table 3-c

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Table 3.d

Starts of Dwelling Units by Principal Source of Financing, 1954-1961.

Item	1954	1955	1956	1957	1958	1959	1960	1961
Public Housing								
Direct Government House-building	1,473	1,975	2,400	2,703	3,478	1,475	1,830	2,778
Private Housing Assisted by NHA								
NHA Loans made by CMHC								
Limited-Dividend	628	1,416	1,689	4,284	5,608	5,296	1,380	3,551
Other CMHC Loans	587	704	1,023	13,049	30,187	29,933	12,408	20,301
Total CMHC Loans	1,215	2,120	2,712	22,333	35,795	35,229	13,788	23,852
NHA Loans made by Approved Lenders								
Chartered Banks	17,319	33,228	15,367	15,084	24,990	15,015	77	16
Life Insurance Cos.	29,223	26,015	21,346	7,975	15,329	9,940	13,702	19,988
Loan, Trust Cos., etc.	2,277	3,830	3,436	912	4,214	1,641	5,144	15,330
Total NHA Loans made by Approved Lenders	48,819	63,073	40,149	23,971	44,533	26,596	18,923	35,334
Private Housing Not Assisted by NHA								
Conventional Loans made by Approved Lenders								
Life Insurance Cos.	17,255	22,244	23,923	20,340	24,989	29,562	25,741	24,347
Loan, Trust Cos., etc.	15,636	13,755	11,764	12,526	17,940	15,636	14,375	13,969
Total Conventional Loans made by Approved Lenders	32,891	35,999	35,687	32,866	42,929	45,198	40,116	38,316
Government Assistance Other than NHA	2,269	2,328	1,880	1,808	1,969	2,251	2,115	1,903
Other Financing	26,860	32,781	44,483	38,659	35,928	30,596	32,086	23,304
Total	113,527	138,276	127,311	122,340	164,632	141,395	108,858	125,577

Source: Data for years 1955-1961 are from CMHC's "Canadian Housing Statistics" 1961, Table 35. Data for 1954 are from "ibid" 4th Quarter 1960, Table 32.

Table 3.4

Uses of Dwelling Units by Principal Source of Financing, 1954-61.

Table 3.e

Percentage Distribution of Starts of Dwelling Units by Principal Source of Financing, 1954-1961.

Item	1954	1955	1956	1957	1958	1959	1960	1961
Public Housing								
Direct Government House-building	1.3	1.4	1.9	2.2	2.1	1.0	1.7	2.2
Private Housing Assisted by NHA								
NHA Loans made by CMHC								
Limited-Dividend	.6	1.0	1.3	3.5	3.4	3.7	1.3	2.8
Other CMHC Loans	.5	.5	.8	14.8	18.3	21.2	11.4	16.2
Total CMHC Loans	1.1	1.5	2.1	18.3	21.7	24.9	12.7	19.0
NHA Loans made by Approved Lenders								
Chartered Banks	15.3	24.0	12.1	12.3	15.2	10.6	.1	.0
Life Insurance Cos.	25.7	18.8	16.8	6.5	9.3	7.0	12.6	15.9
Loan, Trust Cos., etc.	2.0	2.8	2.7	.7	2.6	1.2	4.7	12.2
Total NHA Loans made by Approved Lenders	43.0	45.6	31.6	19.5	27.1	18.8	17.4	28.1
Private Housing Not Assisted by NHA								
Conventional Loans made by Approved Lenders								
Life Insurance Cos.,	15.2	16.1	18.8	16.6	15.2	20.9	23.6	19.4
Loan, Trust Cos., etc.	13.8	9.9	9.2	10.2	10.9	11.1	13.2	11.1
Total Conventional Loans Made by Approved Lenders	29.0	26.0	28.0	26.8	26.1	32.0	36.8	30.5
Government Assistance Other than NHA	2.0	1.7	1.5	1.5	1.2	1.6	1.9	1.6
Other Financing	23.6	23.8	34.9	31.7	21.8	21.7	29.5	18.6
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Calculated from data in Table 3.d.

Table 3.f

Starts of Dwelling Units by Principal Source of Financing, 1954-1961

Item	Dwelling Units	%
Public Housing		
Direct Government Housebuilding	18,112	1.7
Private Housing Assisted by NHA		
NHA Loans made by CMHC		
Limited-Dividend	23,852	2.3
Other CMHC Loans	113,192	10.9
Total CMHC Loans	137,044	13.2
NHA Loans made by Approved Lenders		
Chartered Banks	121,096	11.6
Life Insurance Companies	143,518	13.8
Loan, Trust Companies, etc.	36,784	3.5
Total NHA Loans made by Approved Lenders	301,398	28.9
Private Housing Not Assisted by NHA		
Conventional Loans made by Approved Lenders		
Life Insurance Companies	188,401	18.1
Loan, Trust Companies, etc.	115,601	11.1
Total Conventional Loans made by Approved Lenders	304,002	29.2
Government Assistance Other than NHA	16,613	1.6
Other Financing	264,697	25.4
TOTAL	1,041,866	100.0

Source: Calculated from data in Table 3.d.

Table 3.2

Sources of Low Income Loans by Principal Purpose of Fiscal Year, 1974 (cont.)

Direct Government Production/Farming		
Private Housing Assisted by FHA		
FHA loans made by CMHC		
Total CMHC loans		
FHA loans made by Approved Lenders Chartered Banks Life Insurance Companies Loan, Trust Companies, etc.		
Total FHA loans made by Approved Lenders		
Private Housing Not Assisted by FHA		
Conventional loans made by Approved Lenders Life Insurance Companies Loan, Trust Companies, etc.		
Total Conventional loans made by Approved Lenders		
Government Assistance Other than MHA		
Other Financing		

Source: Calculated from data in Table 3.d.

CHAPTER 4

THE USE OF MORTGAGE FUNDS FOR PURPOSES OTHER THAN THE FINANCING OF NEW HOUSE BUILDING

4.1 New house building must compete with other activities for the use of mortgage funds. On the residential side there is a large amount of mortgage lending on the security of existing property, as distinct from new property. And on the non-residential side mortgage loans are made to finance new construction and are also made on the security of existing property.

4.2 Table 4.a indicates that in the period 1954 to 1961, new residential construction absorbed only 8.1 billion or 38% of the total amount of mortgage loans made in Canada. Other uses, the financing of existing residential property, and the financing of non-residential property, both new and old, absorbed the other 62% of the available mortgage funds.

4.3 The presentation on a gross basis seriously underestimates the importance of new residential construction as a claimant of available mortgage resources however. The creation of debt on new residential property represents a net increase of debt equivalent to the amount of mortgage loan, and requires the release of mortgage funds to the borrower in an amount equal to the loan amount. This is not true of first mortgage loans made on the security of existing residential property, most of which is already encumbered, and sometimes

CHAPTER 4

THE USE OF MORTGAGE DEBT FOR INVESTMENT

heavily, with mortgage debt. In this case the net release of mortgage funds is equivalent to the difference between the amount of the new loan and the amount of the existing encumbrance.

4.4 On the average, a dollar of mortgage loan on existing property makes a smaller claim on the net mortgage resources available than does a dollar of loan on new property.

4.5 Of the 13 1/2 billion of mortgage lending that was done from 1954-1961 for purposes other than new residential construction, a large proportion was on existing property although the detailed composition is not known. It is doubtful if as much as $10 billion of this 13 1/2 billion represented a net claim on actual mortgage cash.

4.6 Therefore, because some significant proportion of the proceeds of mortgage loans made on the security of existing property, are actually used immediately to retire existing mortgage debt, the significance of new residential construction as a claimant for available mortgage resources, is much greater than the 38% indicated by the gross flow proportion over the period 1954-1961. A figure near 50% would probably give a better indication.

Type of Lender and Type of Loan

4.7 The Federal Government and the banks concentrate virtually all their mortgage lending in the new residential construction field, since the Government does the great bulk of its lending under the National Housing Act, and the banks are not permitted to lend

except under the Act.

4.8 The life insurance and the loan and trust companies also concentrate heavily on new residential construction. Table 4.d indicates that 58% of the value of their mortgage commitments was for new housing. Over half the remainder was for loans on existing residential property and about one-fifth of their lending was on non-residential property.

4.9 These three sources of funds, then, the Government, the Banks, and the life insurance and loan and trust companies, put up about four-fifths of the mortgage money used for new housing over the period, 1954-1961 (table 4.b). Other lenders, including non-institutional sources and the credit unions, represented the source for over one-half the total supply of mortgage funds but only about one-fifth of the funds used for new housing (Tables 4.b and 4.c). Individuals constitute the largest element in this aggregate of loan sources, and their lending is mainly on existing residential property.

Mortgage Lending On Residential Property, New and Existing

4.10 Borrowers may wish to obtain new mortgage loans on existing residential property for a number of reasons: to refinance a maturing mortgage; to refinance an existing mortgage in order to take advantage of more favourable terms; to raise cash for any of a number of purposes, including the

purchase or repair of the property itself. As a result of the widespread application of regular amortization on conventional as well as on NHA loans, a declining proportion of mortgages on existing property are taken out to refinance maturing mortgage debt. The bulk of these mortgages are occasioned by the sale of property. The individual vendor of property is clearly interested in the availability of credit to the purchaser of his property and through this interest often himself provides mortgage credit either on first or second mortgage account.

4.11 The financing of existing residential property represents the main use competing with new residential construction for mortgage funds. It is true that the mortgage money used to support new residential construction comes largely from different sources than that used for the financing of existing housing. But an increase in the demand for mortgage funds, to finance existing housing, that arose from a desire to obtain cash to spend on things other than housing, would impinge on the demand for new residential construction. It would do this directly by bidding away part of the mortgage funds of life insurance companies, loan and trust companies, and individuals, who might otherwise have financed more new housing. And it would do it indirectly by increasing the amount of mortgage credit that would be required by those potential new house buyers who already own houses and whose entry

into the new house market depends on their ability to sell their present houses.

Table 4.a

Gross Mortgage Flow by Type of Borrower, 1954-1961

Year	Total Gross Mortgage Flow ($ Billion)	New Residential Mortgage Borrowers ($ Billion)	Non-Residential and Existing Residential Mortgage Borrowers ($ Billion)	New Residential Mortgage Flow as percent of Total Mortgage Flow (percent)
1954	1.85	.72	1.13	39%
1955	2.44	.99	1.45	41%
1956	2.83	.99	1.84	35%
1957	2.30	.90	1.40	39%
1958	2.89	1.27	1.62	44%
1959	3.31	1.22	2.09	37%
1960	2.65	.97	1.68	37%
1961	3.16	1.07	2.09	34%
1954-1961	21.43	8.13	13.30	38%

Source: Total Gross Mortgage Flow: Mortgage Registration data from CMHC's "Canadian Housing Statistics" 1961, Table 51.

New Residential Mortgage Borrowers: Estimated from Table 3.a as total expenditures on new housing less outlays on public housing, equities and one half of other financing.

Table 4.b

Source of Funds for Borrowers for New Residential Construction, 1954-1961

Year	Financial Intermediaries (1)		Government		Individuals and Others (2)		Total	
	$ Fillion	%	$ Billion	%	$ Billion	%	$ Billion	%
1954	.42	58%	.09	13%	.21	29%	.72	100%
1955	.71	72%	.03	3%	.25	25%	.99	100%
1956	.75	76%	.03	3%	.21	21%	.99	100%
1957	.52	58%	.07	8%	.31	34%	.90	100%
1958	.68	53%	.34	27%	.25	20%	1.27	100%
1959	.73	60%	.32	26%	.17	14%	1.22	100%
1960	.47	48%	.28	29%	.22	23%	.97	100%
1961	.64	60%	.28	26%	.15	14%	1.07	100%
1954-1961	4.92	61%	1.44	18%	1.77	21%	8.13	100%

(1) Chartered banks, life insurance companies, trust companies and loan companies.

(2) Includes credit unions and pension funds.

Source: Financial Intermediaries: All institutional funds from Table 3.a.

Government: Loans made by CMHC plus other government loans from Table 3.a.

Total: New residential mortgage borrowers from Table 4.a.

Table 1.9

Gross Domestic Fixed Capital Formation at Current Prices

Year	General Government	Public Corporations	Private Sector	Total
	(£ million)	(£ million)	(£ million)	(percentage change)
1948	1.35	0.65	5.00	n.a.
1949	2.04	0.80	4.80	-4.0
1950	2.10	0.90	5.20	+8.3
1951	2.50	1.00	6.00	+15.4
1952	2.80	1.20	6.50	+8.3
1953	3.10	1.40	7.00	+7.7
1954	3.40	1.60	7.80	+11.4
1955	3.90	1.80	8.60	+10.3
1956–1957	4.53	2.14	10.34	n.a.

Source: Central Statistical Office, National Income and Expenditure, 1958, Table 38, p. 46.

Note: Gross domestic fixed capital formation includes additions to the value of existing fixed assets, as well as new construction. Figures are at current prices and are not adjusted for changes in the price level.

Table 4.c

Source of Funds for Non-Residential and Existing Residential Borrowers, 1954-1961

Year	Financial Intermediaries(1)		Government		Individuals and Others(2)		Total	
	$ Billion	%	$ Billion	%	$ Billion	%	$ Billion	%
1954	.24	21%	.06	5%	.83	74%	1.13	100%
1955	.31	21%	.07	5%	1.07	74%	1.45	100%
1956	.38	21%	.11	6%	1.35	73%	1.84	100%
1957	.30	21%	.11	8%	.99	71%	1.40	100%
1958	.35	22%	.14	9%	1.13	69%	1.62	100%
1959	.37	18%	.16	8%	1.56	74%	2.09	100%
1960 *	.50	30%	.19	11%	.99	59%	1.68	100%
1961 *	.56	27%	.19	9%	1.34	64%	2.09	100%
1954-1961	3.01	23%	1.03	8%	9.26	69%	13.30	100%

* Preliminary.

(1) Life insurance companies, trust companies and loan companies.
(2) Includes credit unions and pension funds.

Source: Financial Intermediaries: From (gross) increase in financial intermediaries mortgage portfolio published in CMHC's "Economic Research Bulletin No. 77", Table 1, deduct financial intermediaries new residential construction loans from Table 4.b.

Government: From (gross) increase in governments and government agencies mortgage portfolio, published in CMHC's "Economic Research Bulletin No. 77", Table 1, deduct governments new residential construction loans from Table 4.b.

Total: Non-residential and existing residential mortgage borrowers from Table 4.a.

Table 4.a

| | | |

Table 4.d

Mortgage Loans Approved by Life Insurance Companies, Loan Companies and Trust Companies, 1954-1961

Year	Residential Construction		Non-Residential	Total	Existing Residential as Percent of Total
	New $ Millions	Existing $ Millions	$ Millions	$ Millions	percent
1954	486	144	115	745	19%
1955	548	182	138	868	21%
1956	522	176	141	839	21%
1957	344	150	104	598	25%
1958	509	208	175	892	23%
1959	476	216	216	908	24%
1960	548	221	263	1,032	21%
1961	786	300	298	1,384	22%
1954-1961	4,219	1,597	1,450	7,266	22%

Source: Residential Construction, New: From all residential construction loans of approved lenders, published in CMHC's "Canadian Housing Statistics" 1961, Table 20, deduct mortgage loans approved by chartered banks, "ibid" Table 23.

Residential Construction, Existing: "ibid" Table 20.

Non-Residential: "ibid" Table 20.

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CHAPTER 5

MORTGAGE FLOWS IN RELATION TO OTHER CAPITAL MOVEMENTS

5.1 Mortgages must compete with other long-term investments in the capital market. Lenders of long-term funds can invest in Federal Government bonds, provincial bonds, municipal bonds, corporate bonds, and in some cases in preferred and common shares. The degree to which alternative investments compete with mortgages varies depending on the liability structure of the investing institutions and the laws governing their practices. In general, individuals who provide almost half the flow of mortgage funds are least regulated in their choice of investments, while chartered banks are the most regulated sector. The life insurance companies, the loan companies and the trust companies, fit somewhere in between these two extremes.

Total Long-term Capital Flows

5.2 Table 5.a shows that mortgages represented $7.73 billion out of the $23.46 billion net flow of long-term funds through the capital market in the 1954-1961 period. The mortgage flow thus represented 33 percent of all long-term capital market flows. It fluctuated from a high of 52 percent during 1956 to a low of 16 percent during 1957. In aggregate over the period the net mortgage flow was almost equal to the combined net flow of federal, provincial and municipal obligations.

5.3 The earliest indication of changes in the flow of

CHAPTER 5

MORTGAGE FLOWS IN RELATION TO OTHER CAPITAL

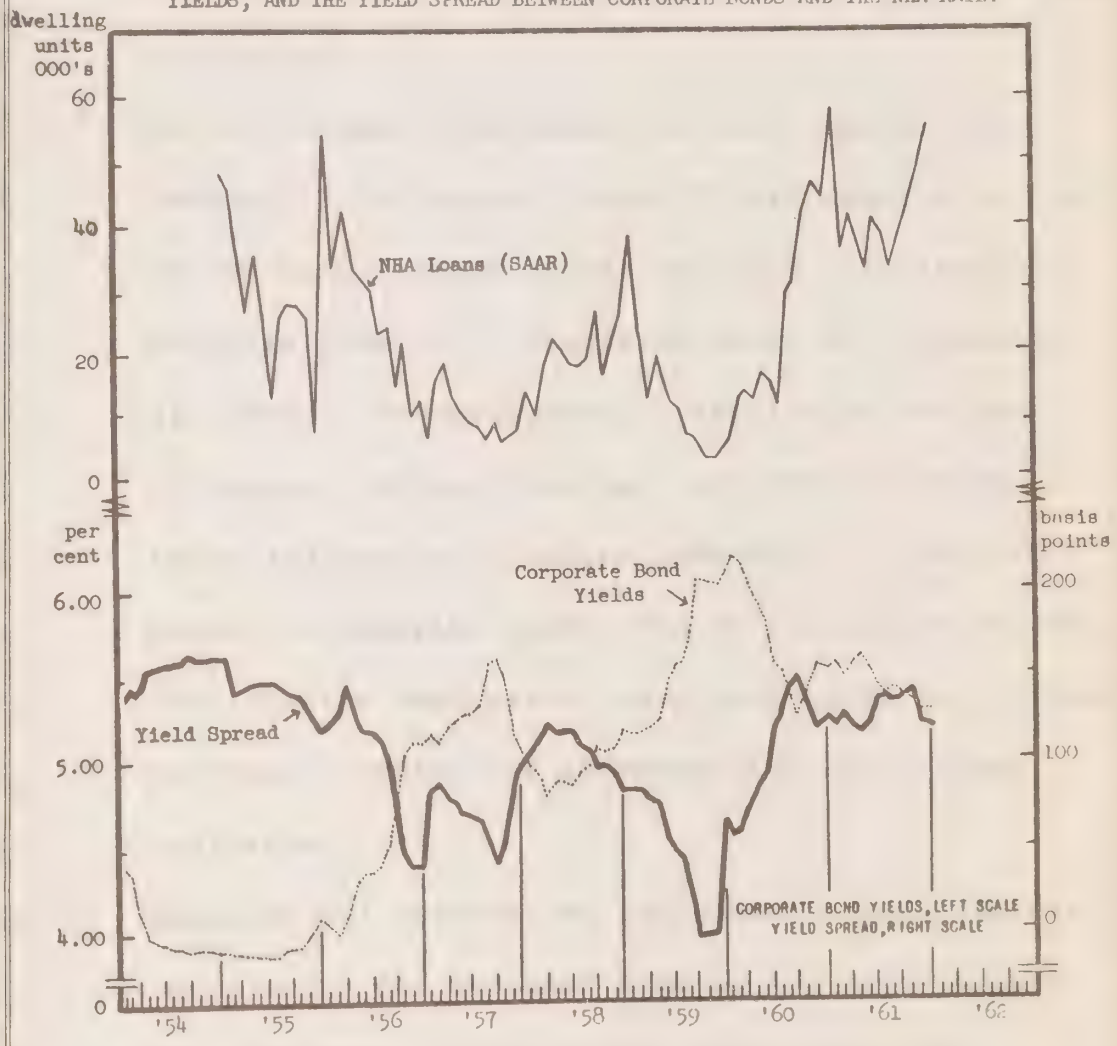
mortgage funds is provided by mortgage approval data, which measure the volume of mortgage loans that lenders undertake to provide. Changes in the capital market which affect the mortgage market, will thus affect that market via the lenders' decision to either contract or expand their approvals of new mortgage loans. The mortgage flow comes however from a diverse group of lenders. Three groups will be considered here, namely the life insurance and the loan and trust companies, the chartered banks, and CMHC.

Life Insurance and Loan and Trust Companies

5.4 The life insurance companies, and the loan companies and trust companies adjust both the volume of their mortgage lending and the composition of that lending as between NHA and conventional mortgages. Table 5.b shows their annual approvals. The data indicate that mortgage lending by these institutions increased very little in the years when interest rates increased, 1956, 1957 and 1959. The NHA lending pattern was much more volatile than that of conventional lending and showed a much more definite tendency to vary counter to the course of interest rates.

5.5 The chart below shows the NHA loan approvals of these institutions in relation to the difference between the NHA interest rate and interest rates on long-term corporate bonds. The tendency for this gap in interest rates to vary counter to the general trend of interest rates is also shown in the chart and reflects the inflexibility of the NHA rate in relation to other long-term yields.

LIFE COMPANIES, TRUST COMPANIES AND LOAN COMPANIES NHA LOANS, CORPORATE BOND YIELDS, AND THE YIELD SPREAD BETWEEN CORPORATE BONDS AND THE NHA RATE.



Source: NHA Loans, CMHC;
Corporate Bond Yields, McLeod, Young, Weir and Company

The Mortgage Flow from Chartered Banks

5.6 Chartered banks are empowered to make NHA mortgages only. Changes in capital market conditions will thus be reflected only in their total flow of mortgage funds and cannot affect the composition of their mortgage flow. Table 5.c contrasts their mortgage commitments with those of the other private NHA lenders.

5.7 As can be seen from Table 5.c their pattern of lending in the period 1954-1959 was similar to that of non-bank lenders except for 1957. During 1957 mortgage lending by chartered banks was increased as a result of moral suasion applied by the Bank of Canada. We can thus say that both chartered banks and non-bank lenders responded in the same manner to changing conditions in the capital market but that the response of chartered banks was stronger both when lending was increased and when it was contracted.

5.8 Banks to all intents and purposes stopped originating loans under the National Housing Act late in 1959. This happened before the NHA rate itself was increased from 6 percent to 6 3/4% in December of 1959, and the withdrawal of the banks was not caused by the increase in the NHA rate since banks are free to originate loans at less than the maximum rate of interest. However, with earnings of 6% or close to it available to banks on shorter term credit or on more liquid investments than mortgages, the origination of 6% NHA loans became unappealing.

The Mortgage Flow from Central Mortgage and Housing Corporation

5.9 The mortgage flow forthcoming from Central Mortgage and Housing Corporation does not respond in the same way to changes in capital market conditions as the flow from the private lenders. Table 5.d contrasts CMHC commitments with the NHA commitment from the private lenders.

5.10 Central Mortgage did not enter the mortgage market as a lender of significant proportions until late in 1957. While CMHC lending in 1958 was greater in total than that of 1957 this represented the first full year of heavy CMHC lending and was at a lower annual rate than that begun in the autumn of 1957. The private lenders heavily increased their lending from 1957 to 1958 and reduced it from 1958 to 1959. CMHC held its lending virtually unchanged from 1958 to 1959, and like the private lenders reduced its lending in 1960 and increased it in 1961. Government lending, therefore, by CMHC, has not been consistently counter to the pattern of private lending nor consistently in phase with it. Lending by CMHC, as a residual lender on the basis of a fixed policy would have tended to produce a pattern of lending counter to that of the private lenders. The basis on which CMHC acted as a residual lender changed throughout the period however, as described in Chapter 3.

Total Mortgage from Lending Institutions and CMHC

5.11 The mortgage flow forthcoming from lending institution

5.9 The mortgage flow for housing from central life insurance and Housing Corporation does not respond in the same way to changes in capital market conditions as the flow from the private lenders. While building societies could accommodate with the May announcement

5.10 Central Mortgage did not enter the mortgage market as a lender of significant proportions until late in 1967. While CMHC lending in total then of 1957 was responsible for about half of the CMHC lending and was a lower annual rate at that point in the annual of 1957. The private lenders nearly increased their lending from 1957 to 1959 and reduced it thereafter to 1963. CMHC held its lending relatively unchanged from 1959 to 1963, as like the private lenders reduced its lending in 1960 and increased it in 1961. Government lending, therefore, CMHC, has been consistent counter to the pattern of private lending for conventional mortgages with it. Lending by CMHC under a federal housing on the basis of a three-tiered rate tended to provide a partial insulation to the effect of the private market. The borrowers in CMHC market is a specialized lender, therefore,

5.11 The mortgage flow that

and Central Mortgage and Housing Corporation, whose component parts were described above is summarized in Table 5.e.

5.12 The $10 billion mortgage commitments by the financial institutions and Central Mortgage and Housing Corporation during the 1954-1961 period represented 47% of the $21.4 billion new mortgages registered in the same period. Generally speaking it can be said that the private lenders adjusted to changing capital market conditions by reducing their mortgage lending during periods of rising interest rates, and increasing their mortgage lending in periods of falling interest rates. This adjustment fell mainly on the NHA component of their mortgage lending.

5.13 The NHA lending potential from private sources has since 1959 been reduced as a result of the chartered banks withdrawal from NHA lending. Partly because of this withdrawal the residual lending from Central Mortgage and Housing Corporation has remained at high levels.

Table 5.a

Net New Capital Market Issues, 1954-1961

Year	Federal Government Bonds (except Treasury Bills)	Provincial Bonds	Municipal Bonds	Corporate Bonds	Stocks (preferred and common)	Mortgages	Total
1954	-.30	.29	.24	.45	.17	.67	1.52
1955	.34	.21	.23	.32	.46	1.18	2.74
1956	-.62	.54	.22	.79	.69	1.73	3.35
1957	-.12	.55	.28	.95	.52	.40	2.58
1958	1.38	.61	.34	.66	.31	.88	4.18
1959	.14	.57	.30	.11	.40	1.35	2.87
1960	.70	.48	.39	.28	.23	(1) .52	2.60
1961	.99	.93	.21	.25	.24	(1)1.00	3.62
1954-1961	2.51	4.18	2.21	3.81	3.02	7.73	23.46

(1) Preliminary.

Source: Mortgages: Central Mortgage and Housing Corporation "Economic Research Bulletin No. 77, Unpublished Supplement", Ottawa, October, 1960.

All other issues: Bank of Canada "Statistical Summary", Ottawa, March, 1962, pps. 168-170.

Table 5.b

Mortgage Commitments
from Life Insurance Companies and Loan and Trust Companies

Period	NHA Mortgage Commitments ($ Millions)	Conventional Mortgage Commitments ($ Millions)	Total Mortgage Commitments ($ Millions)	NHA as percent of Total (percent)
1954	306	440	746	41%
1955	313	556	869	36%
1956	267	572	839	32%
1957	105	493	598	18%
1958	219	673	892	25%
1959	133	775	908	15%
1960	241	792	1,033	23%
1961	453	931	1,384	33%
1954-1961	2,037	5,232	7,269	28%

Source: NHA Mortgage Commitments: CMHC's "Canadian Housing Statistics" 1961, Table 23.

Conventional Mortgage Commitments: CMHC "ibid" Table 22.

Table 5.c

Mortgage Commitments from Chartered Banks and Other Private NHA Lenders

(Millions of Dollars)

Period	Chartered Banks	Non-Bank Lenders	Total Private Lenders
1954	158	306	464
1955	326	313	639
1956	158	267	425
1957	173	105	278
1958	300	219	519
1959	175	133	308
1960	1	241	242
1961	-	453	453
1954-1961	1,291	2,037	3,328

Source: CMHC's "Canadian Housing Statistics" 1961, Table 23.

Table 5.d

NHA Mortgage Commitments of CMHC and Private Lenders

(Millions of Dollars)

Period	CMHC	Private Lenders	Total
1954	27	464	491
1955	18	639	657
1956	20	425	445
1957	235	278	513
1958	389	519	908
1959	367	308	675
1960	168	242	410
1961	271	453	724
1954-1961	1,495	3,328	4,823

Source: CMHC's "Canadian Housing Statistics" 1961, Table 23.

Table 5.e

Mortgage Commitments of Lending Institutions and CMHC

(Millions of Dollars)

Period	NHA			Conventional	Total
	CMHC	Private Lenders	Total		
1954	27	464	491	440	931
1955	18	639	657	556	1,213
1956	20	425	445	572	1,017
1957	235	278	513	493	1,006
1958	389	519	908	673	1,581
1959	367	308	675	775	1,450
1960	168	242	410	792	1,202
1961	271	453	724	931	1,655
1954-1961	1,495	3,328	4,823	5,232	10,055

Source: NHA: CMHC's "Canadian Housing Statistics" 1961, Table 23.

Conventional: CMHC "ibid" Table 22.

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CHAPTER 6

POLICY ISSUES IN THE MORTGAGE MARKET

6.1 In the foregoing chapter the dependence of the new house building industry on the mortgage market has been pointed out; the degree to which new house building activity must compete with other uses of mortgage funds has been discussed; and some broad indication given of the considerable quantitative importance of mortgage borrowing in relation to other demands for long term capital.

6.2 The amount of new housing produced in Canada over the next decade will depend, among other things, on the supply of long term capital available for all purposes, the share that can be attracted by the mortgage market as a whole, and by mortgages for new housing in particular. Given a fixed objective about the amount of new house building that should take place, and given powers of divination into the future course of the capital market as a whole, and the mortgage market within it, one could arrive at a judgment about the capability of the capital market to meet the fixed housing objective. And this could lead to a judgment about a variety of institutional or legislative arrangements which might be made in order to secure the desired housing objective.

6.3 Such a critique of the capital market would suffer from three main defects.

6.4 First, it would depend on a more or less categorical judgment about the correct size of the future

POLICY ISSUES IN THE MORTGAGE

6.1 In the foregoing chapter the dependence of the new
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housing program. The Act itself does not provide an explicit directive on this point. At the end of Chapter 1 of this brief it was suggested that there are certain minimum criteria which are apt to be used to judge the adequacy of the new housing program in relation to objectives implicit in the National Housing Act. But these criteria are presumptive; and they are arguable by reasonable people. Even if they were not, and could be accepted as having some kind of manifest validity, there still would remain the task of coming to a positive judgment about the future course of the various factors which are said to determine the minimum suitable housing program, net family formation, immigration, urbanization, the formation of non-family households. Most of these forecasts would be about demographic phenomena and the degree of past success in forecasting such events does not encourage a strong commitment to current forecasts. Again at the end of Chapter 1 there is an estimate of the "possible" minimum needs for new housing in Canada over the next decade. It is one thing to suggest the likely area of magnitude of these needs largely for illustrative purposes; it is quite another to use such forecasts as a basis for advocating changes in some of the institutional or legislative arrangements that affect the Canadian capital market.

6.5 The second defect of this approach to an appraisal of present capital market arrangements lies in its

commitment to a positive forecast about the trend of events in the capital market itself and in the mortgage market in particular. Minor variations in assumptions about the likely rate of asset growth of the major mortgage lending institutions, and about their investment in mortgages as against other capital market instruments, can produce major variations in conclusions about the amount of mortgage money that will be forthcoming from the institutions in the future. As a result, the adoption of two different sets of assumptions, neither of which on the face of it appear unreasonable, could lead to two opposed conclusions about the capacity of the capital market to secure housing objectives. Judgments about actual institutional and legislative arrangements in the capital market should not depend on small and difficult distinctions in forecasting assumptions.

6.6 The third defect of the procedure is in its narrow partiality. It rests on an evaluation of the capital market from the point of view of its impact on the output of a single durable good. The dispensations of the long term capital market affect the pattern of output of a whole range of durable goods, and they affect also the output of all durable goods together as distinct from less long lived products. The capital market cannot be judged solely by its effects on the production of one particular product. If the claim staking approach is valid for housing, its validity may

be argued for other things as well. And if it is valid for everything then there must be some correct pattern of output of the investment goods whose production is influenced by the capital market. If there is such a proper pattern and scale of output of investment goods, then the institutions and practices which institute the capital market as we know it, are otiose, for they have the main purpose of influencing and modifying and helping to determine precisely this thing.

6.7 This is not to say that the practices and institutions and legislation which comprise our present capital market are unassailable or even satisfactory. The capital market may well be subject to discernible biases and incapacities which it is considered important to correct. From the specific point of view of the mortgage market, lenders may be subject to constraints that they do not face in non mortgage investments, and within the mortgage market the constraints may vary between different kinds of mortgage borrowers and different kinds of lenders. Over past years, certain features of the mortgage market have drawn comment from a variety of sources: the use of an administered interest rate on insured loans under the National Housing Act; the existence of one set of borrowing terms for those buying new housing under the National Housing Act and a different set of terms for those buying existing housing; the confinement of mortgage lending by the chartered banks to NHA loans; the effect of

the 6% interest rate limit, contained in the Bank Act, on mortgage lending by the banks; the legal constraints on the mortgage loan to value ratios that may be offered by conventional institutional mortgage lenders; the rudimentary state of the secondary market for mortgages. The remainder of this chapter contains comment on each of these issues.

The Interest Rate under the National Housing Act

6.8 The maximum interest rate on insured loans under the National Housing Act is set by the Governor-in-Council. The Governor-in-Council may change the rate as frequently or as infrequently as is desired, but Section 4 of the Statute stipulates that at the time it is set it may not exceed the yield on long term Government bonds by more than 2-1/4%.

6.9 The interest rate charged on these loans has tended to be much less flexible than other rates of return available to lenders on long term investments (see Chart on page 36). And for this reason the amount of lending by private lending institutions under the Act has fluctuated more than it would have with a free or readily adjusted rate. The instability of private mortgage lending under the National Housing Act is cited often as the main source of instability in new house building. Table 3.d to Chapter 3 of this brief supports the view that housing starts financed principally by private insured loans under the Housing Act were highly volatile in the period of 1954-1961, and

that total housing starts varied in the same direction as the private NHA loan component. Chapter 5 supports the view that variations in the volume of private NHA lending were influenced in an important way by the comparative inflexibility of the NHA interest rate.

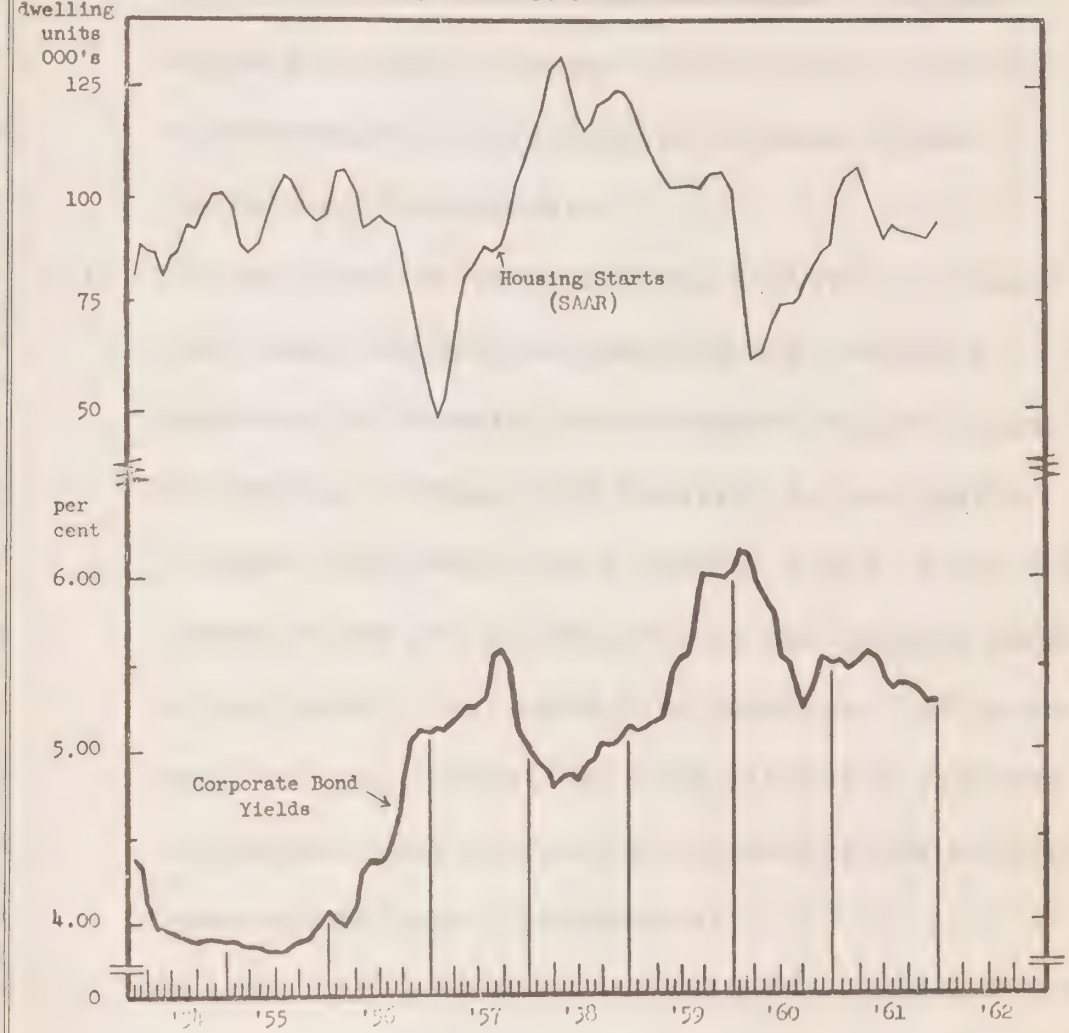
6.10 It is probably true that a more flexible NHA interest rate under the Act would have reduced the instability of private insured lending, but it is doubtful if the overall instability of house building would have been reduced to the same degree. Interest rate rigidity under the Act tends to concentrate variations in lending into the NHA sector. When mortgage money supplies are under pressure, lenders tend to shift their emphasis from NHA to conventional loans, where higher returns may be obtained. A one for one shift is of course not possible since the higher down payment requirements and higher loan charges in the conventional sector make it impossible for all rejected NHA applicants to avail themselves of conventional loans, but there is some tendency for declines in NHA private lending in such periods to be offset in part by a shift in loans from the NHA to the non-NHA sector. When mortgage money supplies are ample, on the other hand, a reverse shift can take place because of the excess demand condition in the NHA sector. To a degree then interest rate rigidity under the Act sector tends not so much to create variations in house building

as to shift the locus of variations to the NHA sector. Under almost any circumstances, and even if all interest rates were free and unrestricted, wide swings in the demand for non-residential long term funds would produce variations in house building. But since shifts between the NHA and the conventional loan sectors are not completely offsetting, it is fair to conclude that interest rate rigidity under the Act has contributed to instability in house building in general.

6.11 The instability of private insured lending under the NHA has at times been defended as an automatic anti-cyclical device. The tendency for housing starts in total to move counter to movements in long term interest rates is indicated in chart on the next page.

6.12 These long term rates themselves, however, behave generally as laggers over the course of the business cycle, the series on starts lags behind the course of interest rates, and construction activity lags behind starts. In the absence of a reliable series on new residential building activity in terms of value of construction put in place the extent of this latter lag is not easy to establish, but it is known that the period of construction of a new single family dwelling averages from 5 to 6-1/2 months depending on the season, and that the average construction period for rental dwellings is customarily longer, 8 to 10 months. Therefore, peaks in new residential construction activity are likely

HOUSING STARTS AND CORPORATE BOND YIELDS



Source: Housing Starts (SAAR) centres with 5,000 population and over, CMHC.
Corporate Bond Yields; McLeod,Young,Weir and Company.

to lag peaks in starts by as much as 4 months and the starts themselves may lag the course of overall activity by a further period depending on the lag in the response of lenders to interest rate changes and the lag of interest rates themselves. These lags would tend to make it hazardous to depend on the statutory interest rate of itself to introduce an appropriate contracyclical pattern to new residential construction.

6.13 To the extent however that the statutory interest rate under the National Housing Act created a condition of chronic excess demand for NHA funds during the 'fifties', it resulted in a situation in which Government, as a lender, could at any time introduce its own funds into the new housing market on very short notice and have assurance that starts would quickly follow. In this situation only the lag between loan approval and construction activity needed to be taken into account.

6.14 Whatever the effects of the statutory interest rate on variations in house building activity, and on the business cycle, over the long run it has tended to limit the participation of the private lenders under the Act. Since the interest rate is set as a maximum, and since lenders are free to offer NHA loans at interest rates less than the maximum it could not result in an excess supply of private funds and therefore it has the effect of restricting the supply of private funds for NHA loans or it has no effect at all. Only for one brief period

under the present Act have loans been available at rates lower than the maximum. This was during the summer of 1955 shortly after the new Act came into force and it followed the entry of the chartered banks as approved lenders under the Act.

6.15 A more flexible NHA rate, if it were thought desirable, could be achieved in at least three ways: it could be done by changing the NHA regulations to allow lenders to originate loans at a discount; it could be done by changing the statute to free the rate altogether; or it could be effected under present arrangements by changing the rate more often.

6.16 It would be possible to maintain the statutory interest rate system and allow lenders to originate mortgage loans at a discount. Such a course might appear contradictory at first sight because the rationale of a fixed contractual rate of interest might be thrown into doubt by a system of discounting which permitted variations in the actual rate of return paid by borrowers. Free contractual rates however, and fixed contractual rates accompanied by discounts are not identical in their effect. A lender seeking a higher return when contractual interest rates are free to move, merely has to raise his contractual rate. If he seeks the same increase in return through a discount he lowers the actual mortgage amount advanced and the borrower thereby has to make a larger down payment. While the yield effects are the same to the lender the demand effects on borrowers are different. The

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into the mortgage market on a large scale.

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A lender awaiting a higher return when contractual
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the actual mortgage amount advanced and the borrow
thereby has to make a larger down payment. What
the yield requires are two terms to the ...

higher down payment requirement associated with the discount technique would characteristically have a more pronounced demand effect than the higher contractual interest rate. Mortgage discounts would cut back the effective demand for loans more rapidly than would rising contractual interest rates. Thus a system of mortgage discounting, while it would more nearly approach a free interest rate position than the present system, would not be identical.

6.17 The present legislation permits the adjustment of the rate at the discretion of Government. In theory at least this discretionary control will allow any degree of flexibility considered desirable by Government. For Government to abandon this system, if it were firmly convinced of the desirability of a more flexible rate, would mean that it no longer wished to exercise the discretionary authority it now has in this field. It is not within the purpose of this brief to comment on this issue.

The Financing of Existing Housing

6.18 The application of the NHA mortgage lending terms exclusively to new housing in Canada affects the choice between the purchase of new housing as against existing accommodation by home owners. New housing of a given standard and quality, financed under the Act, is accessible to a wider range of income and asset holders than older housing of equal merit. The effects of this asymmetrical feature of the housing market have

been commented upon widely in the last few years. There have been a number of arguments advanced in favour of applying the terms of the National Housing Act to the whole market, old as well as new housing.

6.19 While it might not be feasible to introduce terms identical to the present NHA terms in the market for older housing, particularly with regard to amortization periods, similar terms in other respects would be possible. Even the provisions for amortization periods could be very much the same over a large part of the existing stock since the 25-year loan period which is applied in the case of most NHA loans would be considerably less than the reasonable life expectancy of the bulk of housing in Canada today.

6.20 The arguments for extending the NHA loan terms have varied. Builders have advocated the move in the belief that it would permit the easier and more profitable sale of houses by their present owners and enable more of them to enter the market for new housing. It has been advocated also on the grounds that it would facilitate transfers of existing real estate, and permit a more effective use of the existing stock of dwellings. This in itself would appear to reduce the need for new housing and on the surface seems to be incompatible with the argument advanced first. It is not immediately apparent how a measure that would permit the existing stock of housing to be used

Tavistock Chambers

more effectively and flexibly could at the same time result in an increased demand for new housing.

6.21 Much depends on what is meant by a "more effective use" of the existing stock of dwellings. If this is taken to mean merely a greater ease of transfer of properties from one party to another, then it is still compatible with a reduction in the poulation accommodated by the existing stock, and an increase in the population seeking and demanding new accommodation. If, however, the "more effective use" of the existing stock is taken to mean an increase in the total population accommodated by it in equilibrium, then it is not compatible with an increased demand for new accommodation.

6.22 The application of NHA mortgage borrowing terms to the purchaser of older housing, would make older houses more attractive to purchase in relation to rental housing and in relation to new housing. It would, therefore, tend to increase the demand for older houses. The supply of these houses being fixed, prices would tend to rise. The extent of the price increase would depend in part on the supply of mortgage funds.

6.23 If mortgage money supplies were infinitely elastic then there could be an increase in the price of existing owner occupied houses without any diminution in the supply of mortgage funds available for other purposes, and without any worsening of the terms on which loans would be available for other purposes, including the financing of new housing. Whether

6.21 Much depends on what is meant by a "more efficient use" of the existing stock of dwellings. If this is taken to mean merely a greater ease of transfer of properties from one party to another, then it could conceivably be met by the existing stock, and an increase in the population seeking any dwelling, new or modernised, if however, the "more effective use" of the existing stock is taken to mean an increase in the total population accommodated by it, as appears to be the case when it is not acceptable with an increase in the new accommodation.

6.22 The replacement of MPA mortgages presently held by the "purchaser of older housing", would make older houses more attractive to purchasers in relation to new dwellings, thereby tend to increase the demand for older houses. The supply of these houses being fixed, prices would tend to rise. The effect on the price therefore would depend in part on the supply of mortgage funds.

6.23 If existing mortgages were indistinguishable from those granted on new dwellings, existing owners would be encouraged to use their existing owner occupied houses as a source of mortgage funds without any effect on the supply of dwellings, and without any effect on the demand for new dwellings. Mortgages granted on existing houses would be additional to those granted on new dwellings. Whether

there would be an increased demand for new accommodation would depend on the reactions of tenants and owners respectively to the new mortgage borrowing terms available to buyers of existing housing. If the demand of tenants was more responsive to these new terms than that of owners, tenants would be able to bid away a part of the existing owned stock from the present owners, the existing owned stock would be occupied at greater intensity and there would be less demand for new rental and home ownership accommodation.

6.24 In one respect the demand response of tenants to the more favourable mortgage borrowing terms might be expected to be greater than that of the owners. Tenants on the average have less liquid assets than the owners, and less liquid assets in relation to income. As potential buyers of houses they are more dependent on secondary means of financing and would be affected relatively more than owners by increased opportunity to substitute first mortgage money for money borrowed from second mortgage or similar sources. This suggests that tenants would be able to effect a net shift into the owner occupied accommodation and that this accommodation would be occupied more intensively with rents declining and the offer prices for new houses declining.

6.25 There would however be a source for increased demand for housing space on the part of owners, and on that the tenants would not share. The owners would enjoy an increase in wealth as a result of the bidding up

of the prices of existing owned housing. At the outset this increase would be in the form of increased housing equity. The owners would be in a position to translate this increased wealth into other forms including increased command over dwelling space and to the extent that they did so, could offset, or even reverse any net shift of tenants into the present owned stock of dwellings. The owners' wealth effect might be great enough to result in a net reduction of the population occupying the existing owner occupied stock and a consequent increase in the demand for new rental and owner occupied accommodation.

6.26 Even on the assumption then that mortgage money supplies are infinitely elastic, it is possible, but by no means certain that the application of NHA borrowing terms to the existing housing stock would bring about an increased demand for new housing. Mortgage money supplies of course are not infinitely elastic. Inelasticity in mortgage money supplies would tend to reduce the chances that an increased demand for new housing would result from the application of NHA borrowing terms to the used housing market. It would do this by worsening the borrowing terms that would be available for financing new housing, and by diminishing the increase in the price of existing housing from which derives the wealth effect which in turn holds the only hope for an increased demand for new accommodation.

6.27 The application of NHA borrowing terms to the used housing market would in theory mean the availability of NHA loan to value ratios, interest rate, and amortization periods for the existing house market. As far as the private mortgage lenders are concerned such terms cannot simply be made available by Government fiat. The supply of private funds available at these terms is probably almost fixed at any one time, and to make funds available at these terms for transactions in the existing house market would merely make them that much less available for financing new housing. This in turn would tend to diminish the demand for new housing accommodation, or at least the demand that could be made effective by the provision of mortgage funds. A fixed amount of private funds at the terms stipulated would also limit the occasions on which owners of existing housing could actually realise a wealth increase, and this also would diminish the possibility of an increase in the demand for new housing. It would be possible to achieve some increase in the supply of private mortgage money by increasing the interest rate which lenders could charge under the National Housing Act, but this policy would also worsen the terms available to borrowers for financing new housing, and it would diminish the wealth effect.

6.28 It would be possible for Government to achieve a close approximation to infinite elasticity in the supply of mortgage funds by itself undertaking,

as a residual lender, to meet the whole of the increase in demand for funds that would result from the availability of NHA terms on the existing market. This would imply of course a readiness on the part of the Government, to play a far greater role as a direct mortgage lender than it has over the past five years, to say nothing of the comparatively minor role it played in the years prior to that. It is not just that Government would have an additional role to play as a residual lender in the used housing field. The residual position itself would be amplified by a reduction in the availability of private NHA funds. The private lending institutions, comprising the life insurance companies, and the trust and loan companies have been lending $200 - 300 million annually in recent years on existing residential property. They have been lending these amounts as conventional lenders and have been earning more than the NHA interest rate on such loans. If NHA terms were made applicable to this field it is highly doubtful that even as much money would be forthcoming from present private lenders, and the demand for funds would increase in two ways. There would be a demand for an increased number of transactions and the average loan per transaction would increase. The increase in residual lending by the Government, taken to represent the sum of the increase in the total demand and the decrease in the private supply would be considerable. As suggested above,

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even this degree of elasticity in the supply of mortgage funds could not assure an increase in the demand for new residential construction.

6.29 In summary, those who advocate the application of the NHA terms to the used housing market, as a means to stimulate new house building, are assuming first that there will be on the part of home owners some significant elasticity in the demand for housing space as wealth increases, and they are assuming also that there is a high degree of elasticity in mortgage money supplies, either in the private market itself which seems unlikely, or through Government's presumed readiness to assume a vastly increased role as a residual mortgage lender.

6.30 An opposite viewpoint is arguable however, according to which the NHA terms should apply to existing housing because in all likelihood the move would result in a decreased demand for new construction. If the application of similar mortgage borrowing terms to both the new and the existing house market achieves a redistribution of existing space that results in a reduced demand for new housing, then a part of the existing demand for new housing is attributable purely to asymmetry in the mortgage market, and from a housing point of view, and a resource use point of view, is wasteful. Even on the assumption that the measure would increase demand for new accommodation, it would probably only do so by virtue of a large increase in Government lending at terms more favourable than

would emerge from the private market alone and it could be fairly asked why Government, which lends substantially now to those who can afford new housing, should not do the same for those who buy existing housing.

6.31 The dilemma arises from the basic duality of purpose that underlies housing legislation, housing purposes themselves, and employment. Dollar for dollar new house building directly creates more employment than the transfer of existing property. A high priority for employment objectives would caution against a measure that would reduce the demand for new housing, or would increase this demand only by virtue of an infusion of Government funds that might well have a greater employment impact used in another way. On the other hand, if pure housing considerations predominate, there is less to be said in support of arrangements that tend to achieve housing objectives by the comparatively expensive method of new building, stimulated by devices that give new housing a competitive advantage in accessibility through the terms of mortgage borrowing.

6.32 The question involves not only the distinction between employment purposes and housing aims, but also the distinction between Government as a loan insurer and Government as a lender in housing. It involves therefore not only questions of basic purpose, but also fundamental questions of policy techniques. It is for Government itself of course to decide these basic questions of ends and means.

NHA Mortgage Lending and the Banks

6.33 The chartered banks in Canada are subject to two legislative constraints as mortgage lenders. First they cannot originate mortgage loans except under the National Housing Act, 1954. Second, as lenders under the Act they are subject to the interest rate ceiling of 6% in bank loans contained in Section 91 of the Bank Act. When the NHA interest rate on insured loans is higher than 6%, the chartered banks in practice may not take advantage of it and to the extent that they lend at all, observe the 6% limit imposed by the Bank Act.

6.34 Banks to all intents and purposes stopped originating loans under the National Housing Act late in 1959. With earnings of 6% or close to it available to banks on shorter term credit or on more liquid investments than mortgages, the origination of 6% NHA loans became unattractive. The experience and performance of the chartered banks as NHA loan originators, from 1954 - 1959, was vigorous volatile, and brief.

6.35 Banks may acquire 6-3/4% or 6-1/2% NHA loans on the secondary market, and they may acquire them at prices that promise yields in excess of 6%. But while this might allow some indirect infusion of bank money into the mortgage market, it does not permit the use of the far-flung system of branch banks for the origination of mortgage loans, to which it is so well suited.

6.36 The restriction of bank loan interest rates has

implications far beyond the mortgage market in general however, or the NHA mortgage market in particular. For this reason it is difficult to form conclusions about it from the point of view of mortgages on new housing alone.

Conventional Mortgage Lending Terms

6.37 The life insurance companies, and the loan and trust companies in Canada, who constitute the main source of conventional institutional mortgage money, are subject by law in their conventional mortgage lending to a specific loan limit representing two thirds of the lending value of the property serving as security for the loan.

6.38 This limit means that in making mortgage loans, these lenders are limited in their freedom to offer high level loans and to obtain the higher rates of interest that such loans could presumably command. In a sense the loan ceiling limits the rate of interest that conventional lenders can obtain from borrowers and thereby restricts the ability of mortgage borrowers to lay claim on capital market funds. It constitutes a restriction therefore on the mortgage market considered as a part of the whole capital market.

6.39 The legislation restricting the first mortgage loan levels, however, was not primarily designed to either restrict or expand the mortgage market as such. It was designed primarily to protect the position of the owners of the liabilities of the financial institutions affected, and to prevent

these institutions, as custodians of the savings of the general public, from undertaking undue risks. The general regulation and supervision of financial institutions is not among the responsibilities of CMHC and it is therefore not within the competence of CMHC to comment on all aspects of this question. But CMHC is concerned with the mortgage market in general and with mortgage supplies from these lending institutions in particular. It is perhaps appropriate to suggest that the safety of the savings entrusted to these institutions is related not only to the security of principal but also to the rate of return on their investments, and that maximum loan to value ratios, while they protect principal, sacrifice earning rates. Skill and judgment is required to achieve a proper balance between risk and yield in investment. The years of experience of specialization of the lending institutions would suggest that they more than any other group are qualified themselves to make such choices. However, statutory and regulatory constraints observed by institutional investors in the placement of funds, go far beyond the mortgage market, and because constraints in one sector of the capital market affect the availability of funds in other sectors, their combined effects, even on the mortgage market alone, are not discernible from a consideration of the mortgage loan to value limits. As stated earlier, CMHC is not in a position to comment generally on this question.

A Secondary Market for Mortgages

6.40 Mortgages, as compared with the other main long term capital market instruments, bonds and stocks, have a very restricted secondary market. They are held largely by those who originated them. Recent steps taken by Government in the secondary mortgage market, are discussed in the Annual Report, 1961, of Central Mortgage and Housing Corporation, and for convenience the text is reproduced below.

6.41 "Mortgage investment in Canada has been confined largely to those institutions or individuals that originally make mortgage loans to borrowers. The origination of mortgage loans on a large scale requires special organisation and skills in credit selection, appraisal, and construction inspection, expertise that is quite separate from access to or possession of funds for long-term investment. Partly because of these special administrative requirements, the origination of mortgages by private lending institutions in Canada has been done mainly by life insurance companies, trust companies, loan companies and credit unions, although the banks also began to make loans after the 1954 Housing Act removed the legal obstacles that had earlier prevented their participation. Individuals have also been important in the aggregate as originators of mortgage loans in Canada.

6.42 "A more active secondary mortgage market, by separating the functions of originating and

investing in mortgages, would increase the potential supply of mortgage funds in two ways. First, it would permit the participation of institutional, personal and non-resident investors who are not in a position to originate loans. Second, the liquidity that an active secondary market would impart to the mortgage as an investment, would tend to encourage further mortgage commitments by existing loan originators.

6.43 "The secondary market could separate the function of owning mortgages, not only from that of originating them, but also from that of administering them. A mortgage portfolio characteristically includes a large number of comparatively small loans to separate individual borrowers, each loan subject to combined monthly payments of principal and interest. As compared to bonds or stocks, mortgages are expensive to administer, particularly on a small scale. The development of organisational skills in mortgage administration is not necessary as a condition of mortgage investment, however, since the servicing of mortgage accounts can be performed for a fee by established originators, or by other lenders equipped to do the job. The mechanical problem of mortgage administration, therefore, except as it constitutes a necessary expense, need not prevent the extension of mortgage investment opportunities to those institutions or persons who are not in a position to administer mortgage loans.

6.44 "The National Housing Act of 1954 made provision for secondary mortgage market transactions. Approved lenders originating NHA mortgages were permitted to sell them to other investors, provided the servicing of the mortgages was retained by an approved lender. In this way institutions, and even individuals not organized to originate mortgages, or to administer them, could nevertheless invest in them.

6.45 "In the period 1954-1961 a resale or secondary market for mortgages has developed slowly but surely. In these years, $266 million mortgages were sold by approved lenders out of $3.1 billion mortgages originated by them under the National Housing Act. This means that one out of ten of the mortgages they originated under NHA was resold in the secondary market. On the average, mortgage lenders thus obtained about 9% of the funds they invested in NHA mortgages through the secondary mortgage market.

6.46 "The major proportion of these mortgages was sold to pension funds. These funds purchased $170 million, or two out of three mortgages traded in the secondary mortgage market. At the end of 1960, pension fund assets totalled $3.6 billion, just one-half of the $7.2 billion savings accumulated in chartered banks, and about 45% of the $8.0 billion assets held by the life companies. The absolute growth of pension fund assets, however, at an annual average of nearly $400 million over

the period 1953-1960, has not been much less than that of life insurance company assets and has exceeded the absolute growth of those bank assets which derive from savings deposits. Only 8% of pension fund assets are invested in mortgages compared to 42% for life companies.

6.47 "In addition to pension funds, other corporate borrowers were also drawn into the mortgage market through sales made by approved lenders in the secondary mortgage market. This group of investors acquired $100 million, or one out of three of the mortgages traded in that market. Even individuals purchased a small amount.

6.48 "Progress in secondary market development, while encouraging, has not represented a major amplification of mortgage money supplies. The mere removal of mechanical difficulties associated with the origination and administration of mortgages and the provision of Government insurance against default has not attracted into the mortgage field a massive contribution from investors who had not previously had mortgage lending experience. Mortgages have features, other than the comparatively high costs of origination and administration, that sometimes affect their attractiveness as investments.

6.49 "For one thing, NHA mortgages are subject to voluntary repayment by the borrower after they have run three years. This call privilege means investors may have to accept repayment of mortgages, particularly during periods of falling interest rates, when

borrowers might be prone to repay their debt and precisely when investors would like to retain investments at their original yields.

6.50 "NHA mortgages provide their owner with equal monthly payments of combined principal and interest. While this annuity type of payoff may have advantages for certain kinds of investors, such as pensioners and pension funds, it is unfamiliar to most investors and it tends to accentuate the reinvestment problem for small scale investors.

6.51 "A further difficulty for small investors lies in the inconvenience of the size of individual mortgages. No really small mortgages would be worth having, because of the administrative expense, and indeed for some time there will be few available.

6.52 "The very illiquidity of NHA mortgages, in the absence of a continuous and generally accessible secondary market, itself constitutes a difficulty in the way of more rapid development of such a market.

6.53 "As a compensation for their unique peculiarities, mortgages offer the investor yields that are high in relation to the firmness of security. National Housing Act mortgages in particular are secured not only by the mortgaged property but also by Federal Government insurance against default.

6.54 "On NHA mortgages, the interest return to the lender, even when the costs of loan origination and administration are allowed for, has characteristically

run well above that on long-term Government bonds. The NHA interest rate is set by Government, however, and in the past has not always varied with other interest rates on the market. For one important group of lenders, the banks, there has been no strong incentive to conduct an active selling programme to form the basis of a broader secondary market. NHA insured mortgages acquired by the banks during their first three years of mortgage lending, after the introduction of the new Housing Act early in 1954, were at interest rates from 5% to 5-1/2%. Mortgages acquired from 1957 to 1959 were at 6%. Since late in 1959 the banks have been virtually out of mortgage lending because interest rates had risen to a point where 6% mortgage loans could not compete for their funds with other loans and investments and because, by virtue of the 6% interest rate limit imposed on bank loans by the Bank Act, they were not able to originate loans at the 6-3/4% NHA interest rate established in December of 1959. The rising trend of interest rates since 1956, and the lack of 6-3/4% mortgages from their mortgage holdings, meant that the whole mortgage portfolio of the banks would have been marketable in quantity only at a discount. Apart altogether from difficulties associated with book losses, sales at a discount make sense only if the seller can reinvest the sale proceeds at a yield higher than that implicit in the sale, and sufficientl higher that after meeting the expenses of reinvestment

the seller still emerges with a better yielding asset than the one sold. For the most part, banks, because of the 6% limit on their loan interest rates, have not been in a position to do this, and have not sold a substantial amount of their mortgage portfolios.

6.55 "Life Companies, as would be expected, have been less disposed to sell NHA mortgages than the banks, even though since December, 1959 they have been in a position to originate loans at more than 6%. Their prime interest is in holding loans as investments. This is not to say that they would never sell existing NHA loans in quantity in order to reinvest in new NHA loans or other assets. But in the absence of an organized secondary market for NHA mortgages there are other assets which life insurance companies can more conveniently liquidate if they wish to make new investments beyond the limit imposed by their current cash receipts.

6.56 "Trust and loan companies, in relation to the amount of their lending, have sold more NHA loans than either the banks or the life insurance companies, but they have retained the bulk of their insured loan holdings as investments.

6.57 "Although interest rates on NHA loans are usually judged to be high in relation to those on other long-term investments of comparable security, they have still not been high enough to prompt the spontaneous development of a large private secondary market. This failure is not wholly due to the

peculiar investment features of the mortgages themselves. It is more attributable to the novelty of this type of investment, the inexperience of potential purchaser of NHA mortgages, and an exaggerated notion of the difficulties entailed in mortgage investment. Only experience, education and knowledge about mortgage investment can overcome these obstacles. It was with a view to developing a wider knowledge and experience on the part of mortgage purchasers that the Government, early in the year, took steps in this field.

6.58 "The Minister of Public Works in April, 1961 announced in the House of Commons that "the first step necessary to encourage an active market is to ensure that there is an ample supply of existing mortgages available to interested buyers. Accordingly, the Government has instructed Central Mortgage and Housing Corporation to offer for sale as soon as possible at reasonably attractive yields to investors mortgages now held in its portfolio as a result of the extensive direct lending operations it has undertaken since this Government took office in 1957."

6.59 "The Minister said it was anticipated that the market could develop in two ways: through the sale of blocks of mortgage loans by one institution to another or among pension funds and trusts; and through sales to a new type of company, some of which were already in existence, which would enable the small investor to participate in the mortgage

market through purchase of the debentures or shares of such companies.

6.60 "In accordance with these instructions, the Corporation started to auction part of its NHA mortgage portfolio. Three such auctions were held during 1961, at which a total of $40.7 million in mortgages was sold. One-quarter of these was in the form of options which were subsequently taken up. These $40.7 million in mortgages were sold by tender at which not only the approved lenders and their approved correspondents were invited to bid, but also members of the Investment Dealers' Association of Canada.

6.61 "Some of the mortgages sold were later resold by the purchasers to pension funds that were not previously investors in mortgage loans. Gradually, new pools of accumulated savings are thus beginning to be tapped for mortgage financing. The mortgage auctions held by the Corporation should enable private investors to gain experience in the mechanics of the secondary mortgage market. In time this should lead to a more active market in which mortgages, as bonds are now, will be readily traded on a continuous basis.

6.62 "Government activity in 1961 in the secondary market is based on the expectation that, with the development of greater knowledge and familiarity with mortgages and after the early operations of new private institutions in the field, a market based primarily on private sources of mortgages

will develop. The Corporation's activity in this field is not intended as a device to raise cash for its own lending operations, or for other Government purposes. The secondary market will serve a useful purpose only if it draws into the mortgage field new investors, either directly as mortgage holders or indirectly as holders of the obligations of mortgage investment companies. Access to such private funds -- pension funds, corporate savings, personal funds, non-resident funds and savings which are available only to a very limited extent for mortgage purposes today -- would widen the whole base of mortgage lending in Canada."

APPENDIX A

Schedule 1. Housing Legislation Provisions, Canada, 1918 - 1961

Date	Reference	Legislative Authority	Purpose of Act or Order-in-Council
1918, Dec. 3	P.C. 2997	Order-in-Council under War Measures Act.	".... to create better housing conditions for the residential population of the larger centres of Canada".
1935, July 5	25-26 George V Chapter 58	The Dominion Housing Act, 1935	".... to assist the construction of houses".
1937, Mar. 31	1 George VI Chapter II	The Home Improvement Loans, Guarantee Act, 1937	".... to increase employment by encouraging the repairs of rural and urban homes".
1938, July 1	2 George VI Chapter 49	National Housing Act, 1938	".... to assist in the construction of houses".
1941, Feb. 20	P.C. 1169	Order-in-Council under the Department of Munitions and Supply Act	".... to establish priority regulations including the supply and distribution of construction materials".
1941, Feb. 24	P.C. 1286	Order-in-Council under the Department of Munitions and Supply Act	".... to procure the incorporation of company under the name of Wartime Housing Limited with the intent and for the purpose of renting, purchasing, constructing or otherwise acquiring and providing and generally managing suitable living accommodations to persons engaged in the production of munitions of war and supplies or on defence projects".
1942, Aug. 18	P.C. 7388	Order-in-Council under the Appropriations Act, No. 5, 1942.	".... for the purpose of financing the conversion of existing houses into multiple family houses".
1943, Apr. 1	P.C. 2641	Order-in-Council under the War Measures Act.	"To authorize Minister of Finance to acquire large dwelling units in Ottawa area for conversions". This was the first of the Home Conversion Plan Orders.
1944, Aug. 15	8 George VI, Chapter 46	The National Housing Act, 1944	".... to promote the construction of new houses, the repair and modernization of existing houses, the improvement of housing and living conditions and the expansion of employment in the post-war period".

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Schedule 1. continued.

Date	Reference	Legislative Authority	Purpose of Act or Order-in-Council
1944, Dec. 19	P.C. 9439	Order-in-Council under the War Measures Act.	To establish the Emergency Shelter Regulations.
1945, Dec. 18	9-10 George VI, Chapter 15.	The Central Mortgage and Housing Corporation Act, 1945	".... to incorporate the Central Mortgage and Housing Corporation".
1946, Apr. 23	P.C. 1609	Order-in-Council under the Emergency Transitional Powers Act, 1945	".... for the purposes of maintaining and regulating supplies and services, to vest in the Priorities' officer certain powers respecting construction materials".
1946, Aug. 31	10 George VI, Chapter 61.	An Act to amend the National Housing Act, 1944	Primary industry loans introduced
1947, Mar. 25	P.C. 1095	Order-in-Council under the Income War Tax Act.	To provide accelerated depreciation on rental housing.
1947, June 27	11 George VI, Chapter 40	An Act to amend the National Housing Act, 1944	CMHC empowered to make direct loans where loans unavailable from private lenders.
1948, June 30	11-12 George VI Chapter 63	An Act to amend the National Housing Act, 1944	Rental guarantee loans introduced. CMHC empowered to make direct rental guarantee loans where loans from private lenders unavailable.
1949, Dec. 10	13 George VI, Chapter 30	An Act to amend the National Housing Act, 1944	This amendment provided for Federal-Provincial projects. It also permitted CMHC to make an additional 1/6 loan on top of the usual joint loan.
1951, June 20	15 George VI, Chapter 32	An Act to amend the National Housing Act, 1944	Provided for the interest rate on joint loans to be set by Governor in Council at not more than 2% above long-term (12 years) government bond rate
1953, May 14	1-2 Elizabeth II	An Act to amend the National Housing Act, 1944	Approved lenders expressly authorized to act as agents for CMHC.
1954, Mar. 18	2-3 Elizabeth II	The National Housing Act, 1954	"An Act to Promote the Construction of New Houses, the repair and Modernization of Existing Houses and the Improvement of Housing and Living Conditions"

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Schedule 1: continued.

Date	Reference	Legislative Authority	Purpose of Act or Order-in-Council
1956, June 7	4-5 Elizabeth II, Chapter 9	An Act to amend the National Housing Act, 1954	The insurance authority under NHA was increased from $2,000 million to $4,000 million.
1957, Dec. 20	6 Elizabeth II Chapter 18	An Act to amend the National Housing Act, 1954	CMHC direct lending authority increased from $150 million to $400 million. Lending terms on insured loans eased by raising loan to value ratios.
1958, May 20	7-8 Elizabeth II, Chapter 3	An Act to amend the National Housing Act, 1954	CMHC direct lending authority increased from $400 million to $750 million.
1959, Mar. 20	7-8 Elizabeth II, Chapter 6	An Act to amend the National Housing Act, 1954	CMHC direct lending authority increased from $750 million to$1000 million. NHA mortgage insurance increased from 98 percent to 100 percent. Acquisition fee payable to approved lenders in cases of default increased from $125 to $150.
1960, Mar. 31	8-9 Elizabeth II, Chapter 10	An Act to amend the National Housing Act, 1954	CMHC direct lending authority increased from $1,000 million to $1,500 million. The insurance authority under NHA increased from $4,000 million to $6,000 million.
1960, Dec. 2	9 Elizabeth II Chapter 1	An Act to amend the National Housing Act, 1954	NHA lending terms eased by raising maximum loan amount from $12,800 to $14,900.
1961, Sept. 29	9-10 Elizabeth II, Chapter 61.	An Act to amend the National Housing Act, 1954	CMHC direct lending authority increased from $1,500 million to $2,000 million.

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Schedule 2: NHA Terms of Lending for Single Family Dwellings, 1935-1961

Date	Legislative Authority	Interest Rate	Loan to Value Ratio	Term of Loan	Maximum Loan Amount
		Joint Loans			
1935 Jan. 1	Dominion Housing Act, 1935.	5.00% (Borrower) 5.66% (Lender)	80%	10 years	No limitation
1938 July 1	National Housing Act, 1938.	" "	90% of 1st $2,500 80% of remainder	"	"
1939 Dec. 31	P.C. 4020	" "	"	"	$4,000
1943 Dec. 19	P.C. 11047	" "	90% of 1st $3,200 80% of remainder	"	"
1944 May 11	Statement by Minister of Finance (Hon. J.L. Ilsey) House of Commons	4.50% (Borrower) 5.00% (Lender)	"	"	"
1944 Aug. 15	National Housing Act, 1944	" "	95% of 1st $2,000 85% of next $2,000 70% of remainder	20 years	$6,400
1946 Aug. 31	Statutes of Canada 1946, Chapter 1	" "	"	25 years	"
1947 June 27	Statutes of Canada Chapter 40	" "	95% of 1st $3,000 85% of next $3,000 70% of remainder	30 years	$7,000
1947 Oct. 10	P.C. 4089	" "	"	"	$8,500
1949 Dec. 10	Statutes of Canada 1949, Chapter 30	" "	95% of 1st $3,000 85% of next $3,000 70% of remainder plus 1/6 additional loan	"	$9,917
1951 Feb. 5	Statement in House of Commons by Minister of Resources and Development (Hon. R.R. Winters)	" "	95% of 1st $3,000 85% of next $3,000 70% of remainder 1/6 additional loan suspended	"	$8,500
1951 June 26	P.C. 3344	5.00% (Borrower) 5.50% (Lender)	"	"	"
1951 Dec. 19	P.C. 6804	" "	"	"	$10,000
1952 Aug. 31	P.C. 3907	5.25% (Borrower) 5.75% (Lender)	"	"	"
		Insured Loans			
1954 Mar. 22	National Housing Act, 1954	5.50%	90% of 1st $8,000 70% of remainder	30 yrs.	$12,800
1955 Feb. 16	P.C. 213	5.25%	"	"	"
1956 Mar. 23	P.C. 466	5.50%	"	"	"
1957 Jan. 22	P.C. 90	6.00%	"	"	"

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Schedule 2 - Concluded

Date	Legislative Authority	Interest Rate	Loan to Value Ratio	Term of Loan	Maximum Loan Amount
1957 Dec. 20	Statutes of Canada 1957-58 Chapter 18	6.00%	90% of 1st $12,000 70% of remainder	30 yrs.	$12,800
1959 Dec. 16	P.C. 1584	6.75%	"	"	"
1960 Aug. 4	P.C. 1063	"	"	"	$12,800 (+$500 if fallout shelter included)
1960 Dec. 2	9 Elizabeth II Chapter I	"	95% of 1st $12,000 70% of remainder	35 yrs.	"
1960 Dec. 7	P.C. 1649	"	"	"	$14,200 ($14,900 for four bedrooms or more, +500 for fallout shelter)
1961 Nov. 6	P.C. 1559	6.50%	"	"	"

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Schedule 3: Terms of NHA Rental Lending for Joint and Insured Loans, 1935-1961

Date	Legislative Authority	Interest Rate (to Borrower)	Loan to Value Ratio	Term of Loan	Maximum Loan Amount (per dwell.)
		Joint Loans			
1935 Jan. 1	Dominion Housing Act, 1935.	5.00%	80%	10 years	No limitation
1939 Dec. 31	P.C. 4020	Rental Loans Suspended			
1944 Aug. 15	National Housing Act, 1938.	4.50%	80%	20 years	$4,000
1947 Jan. 1	P.C. 5238	"	"	"	$4,400
1947 June 27	Statutes of Canada 1947 Chapter 40	"	"	30 years	"
1948 July 20	P.C. 3138	"	"	"	$4,800
1949 Dec. 6	P.C. 6129	"	"	"	$6,700
1952 Oct. 30	P.C. 4272	5.25%	"	"	$7,200
		Insured Loans			
1954 Mar. 22	National Housing Act, 1954	5.50%	"	25 years	$7,000 (+80% value of garage.)
1955 Feb. 16	P.C. 213	5.25%	"	"	"
1956 Mar. 23	P.C. 466	5.50%	"	"	"
1957 Jan. 22	P.C. 90	6.00%	"	"	"
1958 Mar. 29	P.C. 456	"	"	"	$8,250
1959 Dec. 16	P.C. 1584	6.75%	"	"	"
1960 Dec. 2	9 Elizabeth II Chapter I	"	85%	35 years	"
1960 Dec. 7	P.C. 1649	"	"	"	$8,750
1961 Nov. 6	P.C. 1559	6.50%	"	"	"

Royal Commission on Banking and Finance

D. B. MANSUR

Hearings held at
OTTAWA

Vol.
44A

Date.
October 17, 1962



Official Reporters
F.J.Nethercut and R.J.Young
Toronto, Ont.

TRANSCRIPTION BY MEMBER
Nethercut & Young
Toronto, Ontario

SUBMISSION BY D.B. MANSUR

To

THE ROYAL COMMISSION

ON BANKING & FINANCE

October, 1962

This memorandum is concerned with some of the main gaps and areas of sluggishness of mortgage financing in the residential field. The remarks are directed primarily to the individual house, rather than to rental units in multiple form. There is emphasis upon conditions in larger urban communities, not only because the gaps and areas of sluggishness appear greater in our cities, but also because information is available in more manageable form.

Although we need rental housing in multiple form to round out our housing stock, the apartment house is essentially a venture in trade by its owner depending upon rental income, even to a point that its financing has more of the characteristics of commercial financing than home owner housing whose construction and financing are clothed with a more substantial public interest.

The development of rental housing in multiple form has been buoyant over the last few years. One has to go back to the Rental Insurance plan of 1948 for artificial stimulus to this sector of new housing. Since then it has been difficult to find an apartment house project which has not proceeded because of the lack of mortgage funds. There may be a time when social implications will seem to be consequent upon an insufficient supply of new multiple residential units. But that is not a problem of today.

In Toronto for example - and other major cities are in very much the same position - apartment house vacancies are of the order of 8% of some 100,000 units.

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But that is not a problem of today.

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There are some 10,000 units under construction. The estimated absorption rate in Metropolitan Toronto is 600 units a month. Oversimplified, there seems to be about a 30 month forward supply of rental units in multiple form.

Reference will be made in this memorandum to gaps and areas of sluggishness in smaller communities and in the rural non farm sector. A preliminary examination indicates that there is wide variation in mortgage conditions in these areas. A preliminary look at one of the wealthy counties in Ontario indicates little in the way of sluggishness and gaps. Indeed, there is evidence to suggest that all legitimate demand for mortgage financing is met by resources within the county itself. On the other hand, less prosperous counties experience in greater degree some of the difficulties which will be recited later in this memorandum. The limited comments about mortgage financing other than in our larger cities is not an indication that difficulties do not exist in the smaller communities and the rural non farm areas. The multiplicity of varying circumstances in these areas requires more comprehensive comment than could be contained in this memorandum.

It is for these reasons that the memorandum pretty well limits itself to gaps and areas of sluggishness in financing the single and semi-detached houses in the larger communities.

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and upon my own observations. In most matters to be discussed, complete data is almost impossible to assemble, and there is some doubt that an exhaustive attempt to do so would be worth while. For instance, it would be helpful to have a base of total residential mortgage indebtedness upon which to work. This has been variously estimated in the range of $12 billion to $14 billion. However, from year to year new mortgage advances can only be accurately established by an examination of every registry and land titles office. Even if this were done, there would be no assurance that funds were fully advanced to the amount of the encumbrance. Even more difficult is the fact that repayments on account of principal are not recorded. Accurate figures are available for some of the institutional investors, and their outstanding balances including Central Mortgage are estimated to be about 50% of the total residential mortgage indebtedness.

Before considering gaps and areas of sluggishness in the residential mortgage financing field as they pertain to detached and semi-detached houses, there are certain explanations which may be helpful.

1. Conditions vary greatly as between communities, parts of a single community, type of house, economic climate and effective demand for houses. Housing and housing statistics are generally measured in national terms. They can be better considered as an integration of many different local conditions and circumstances. The present buoyancy in housing

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demand in Edmonton, Calgary and Ottawa creates a very different set of conditions than presently exist in, say, Windsor and Winnipeg. Although national figures are a measure of overall activity in the country, they are not too meaningful to us in examining gaps and areas of sluggishness. But of necessity many of the remarks in this memorandum must reflect the same kind of generality as is contained in national housing statistics. In addition, the memorandum suffers from emphasis on Toronto examples.

2. Another qualification is this. The limitation of the discussion to detached and semi-detached units is made in full recognition that in the major cities in the Province of Quebec there should be consideration of rental units.

3. The discussion is limited to circumstances in the economic and near economic sectors of housing. The gaps in housing credit involving families who require housing with rental subsidy is not considered. However, many of considerations which will be discussed pertain to that uncertain and wavy line of demarcation between families without the resources to enter the economic market place, those families who think they can do so, and those families who have the resources to clearly qualify in the economic sector.

demand in Edmonton, Calgary and Ottawa create a very different set of conditions than presently exist in, say, Windsor and Winnipeg. Although national figures are a measure of overall activity in the country, they are not too meaningful to us in examining gaps and areas of slackness. But of necessity many of the remarks in this memorandum must reflect the same kind of generality as is contained in national housing statistics. In addition, the memorandum suffers from emphasis on Toronto examples.

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4. One of the difficulties in discussing and assessing the gaps and areas of sluggishness in mortgage financing is a very real and natural difference of opinion between the potential homeowner borrower and the potential lender as to the market value of the property in question and suitable terms of mortgage financing such as amount, interest rate, amortization and term. One the one hand, there seems to be a feeling - induced perhaps by repeated liberalizations of terms under the National Housing Act - that the desire to own a house rather than the financial capacity to do so places a responsibility upon someone - perhaps Government - to make available appropriate mortgage financing to satisfy all such desires. Even yet the occupancy of multiple rental housing in English-speaking Canada as a suitable economic alternative to home ownership has connotations of something less than a proper way of life - save for the carriage trade. The doctrine of salvation being attained only through the home ownership of bricks and mortar seems to have more present popular appeal than does the old fashioned belief that home ownership of a house should be the fruit of past endeavour to make a substantial down payment, as well as future endeavour to pay off the balance of purchase price. This homely philosophy does have the

virtue of providing a measure of security and stability for invested mortgage funds which, after all, are the savings of someone other than the homeowner. Somewhere between these two views must be found a reasonable premise or base upon which gaps and areas of sluggishness in our mortgage lending structure can be measured.

5. Part of the climate in which we must consider gaps and areas of sluggishness in our mortgage structure concerns present conditions in the housing field. Post War housing seems to be in its fourth phase. In the years 1946 to 1949 the problem was one of great absolute shortage in our housing stock, emergency shelter, veteran preferences, overcrowding, a house building industry with insufficient capacity and lack of materials. Then there was the 1950 to 1952 period when the diversion of material for the Korean crisis cut the volume of starts. Then we entered the 1953/1958 period during which great progress was made to fill the backlog of need in the economic sector by the high level of starts. The peak of starts in 1958 caused some indigestion which may have accelerated, but certainly signalled our entry into the fourth phase, which was the change from a seller's to a buyer's market. Presently, housing supply and demand in the economic sector are

in reasonable state of balance, the cost of construction has stabilized, competition is such that the quality of a new small house is at a new high, a shoddy house is almost impossible to sell and the home purchaser is getting better value in relation to income than at any time since 1920. The cost of land and services as a large part of the purchase price remains a problem. These are the circumstances in which we must consider the gaps and areas of sluggishness in our mortgage structure.

In considering gaps and areas of sluggishness, new residential construction is the easiest sector to identify. The widening of a group of institutional lenders and the direct operations of Central Mortgage in recent years has had the effect of reducing the gaps in financing for the new house. Provided that the house meets NHA standards, there appears to be practically universal mortgage coverage in Canada with one exception. In remote single industry towns which used to be known as company towns, gaps have occurred because of a difference of opinion as to the role of the company as a guarantor of NHA loans. It is necessary to ensure that the NHA insurance fund does not accept beyond normal risks. On the other hand, companies sponsoring outlying towns are inclined to feel that the NHA policy should provide for full national coverage without special guarantees by the sponsoring company. These situations are usually resolved, but in the meantime, a gap exists. Gaps other than this are so few and

far between that as a generality, it can be said that there is adequate national coverage by the National Housing Act for houses which meet NHA building standards with borrowers who have the minimum down payments required and income sufficient to meet the monthly payments required by the mortgage.

But there is a very real gap presently existent in connection with mortgages on new houses which do not meet NHA standards. These occur most often in smaller cities and towns and in the rural non-farm areas. They take two forms. There is the house built for the owner where for economic or for other reasons the owner feels that NHA standards are unnecessarily high. Then there is the house being built in whole or in part by the homeowner. Owner labour is a mortgage man's nightmare. Down payment takes the form of sweat equity and is not easily measurable. Then there is the problem that in many cases the house never really gets finished. In some cases local private mortgage funds can be found if the covenant is good, or if there is a wide margin of security. Owner built houses often take the form of a co-operative endeavour. In Nova Scotia there is an orderly manner of financing co-operative housing whether or not owner labour is involved. In the smaller communities in the Province of Quebec the local Caisse Populaire is very effective in financing co-operative housing projects. Caisses Populaires also look after a substantial percentage of individual owner-built houses. Ontario and the Western Provinces with limited benefit of this type of financial

institution have greater trouble in financing these classes of houses.

In summary, although he gaps in the financing of new houses are small in relation to the overall number, the problems occasioned by these gaps are acute for substandard houses and housing which has elements of owner labour. By reason of the very untidyness from a mortgage point of view, it seems that these gaps can best be made good by local private funds or local institutions who are familiar not only with local circumstances, but also with the borrowers.

The main problems in the new house field seem to fall into the category of areas of sluggishness, rather than gaps. Areas of sluggishness are intermittent, rather than continuous. The sluggishness arises from a fluctuating flow of mortgage funds from the institutional lenders in the NHA and conventional fields. In the NHA field there was a recent ready and sufficient flow of funds until June, 1962. An increase in Canada bond yields without a corresponding increase in the maximum rate of interest under the NHA narrowed the spread so that practically every NHA lender has ceased lending save for special situations and token amounts. A combination of a high level of commitments during the first half of 1962 and a sales' market that has not been too buoyant has avoided hardship upon the house building industry up to this time. It is likely that Central Mortgage will be active on direct account between now and the time that an acceptable spread between the yield on Canada bonds and NHA loans is

established.

This condition is not new. The house builders feel that these periods of restraint in the flow of NHA funds have a bad effect upon their organizations. They are happier with a steady flow of NHA funds. During periods of restraint in NHA lending, the house builder places reliance on direct CMHC loans to home owners and upon conventional mortgages provided that he is building a class of house where the amount of down payment is not all important. And the lending institutions are inclined to have more conventional funds at times when they have ceased NHA lending.

The intermittency of the flow of funds is more pronounced in the NHA field than in the conventional field because of the inflexibility of the NHA interest rate structure. NHA Regulation No. 20 makes it quite clear that there shall be a par transaction between lender and borrower. With misgivings, the FHA in the United States operates on a discount system which permits a flexibility sufficient to maintain an evener flow of mortgage funds. But the discount system introduces a number of evils and makes the statutory maximum interest rate established by Congress quite meaningless. It is a nice point as to whether the guarantees under the NHA should be equally applicable to a par transaction at 6½% and to a 6½% transaction discounted to 97 giving an effective yield of 7% on a 14 year basis. The discount system tends to encourage regional differentials in interest rates. Up to the mid 1930's we had very definite regional interest rate differentials.

In large measure through the operation of the NHA we have moved towards a mortgage interest rate structure that is truly national. There may still be some elements of lower interest rates in the east than in the west, but the average differential probably does not exceed one-quarter of one per cent. In the United States we find regional differentials of up to 1%. I make this point because I believe that regional differentials are unhealthy and that a system of discounts in the NHA field would tend to recreate them. On the other hand, a system of discounts would help to maintain an evener flow of NHA funds than we have experienced in the post War years. It would also assist the establishment of a secondary mortgage market.

The question has been raised as to whether an even flow of NHA funds, desirable though it may be to the house builder, is desirable for the economy as a whole. Housing is not faced with the business cycle. Some people say it has a cycle of its own. Others say that housing is contracyclical. In Canada experience of recent years strongly suggests that housing is contra-cyclical. 1954 and 1958 were years when there was a decrease in business investment. Housing in 1954 was very buoyant after allowance is made for the fact that insured loans did not get underway until about May, and 1958 with 168,000 starts was our biggest housing year. Injection of mortgage funds may have had some effect upon these peak housing years. On the other hand, in recent years housing starts by house builders have been determined more by current effective demand than by

availability of mortgage funds. However, housing cycles may be affected by the very changed conditions of a buyer's rather than a seller's market. In earlier years of business recession there was a latent, if not effective, housing demand which is not present today nor in the early prospect.

FINANCING SALE OF EXISTING HOUSES

Perhaps the most important gap in our mortgage lending pattern is the lack of crisp and identifiable means of financing to facilitate the transfer of an existing house from a willing vendor to a willing purchaser at a mutually satisfactory price. The range in financing of this kind is so wide that no pattern of general application can be suggested. There are cases where 100% financing has been arranged and other cases where financing prior to a 30% equity proves to be difficult. In some cases the financing is a combination of a first and second mortgage. In other cases it is a single encumbrance of high loan ratio taken back by the vendor and subsequently held, pledged or sold. Likewise the terms of such financing show wide variation. There is the five year second mortgage with short amortization behind a first. In other cases second mortgages carry as lenient repayment terms as the first mortgage extending over periods of up to 20 years. Some of the second mortgages are for a five year term and others are open in that they can be paid off at any time with or without bonus. Effective interest rates show wide variation. The first mortgage sector of such

financing starts from the lending institution base presently 7% to 7½%. Substandard houses or houses in non favoured areas generally carry a first mortgage interest rate of 1% above the so-called prime rate offered by the lending institutions on houses and in areas to their liking.

In the second mortgage fields effective interest rates are presently in the range of 12% to 15%. Included in such effective rate are all charges over and above tariff legal fees and normal disbursements. At the present time the average rate of interest for second mortgage financing in the Metropolitan Toronto area is of the order of 13½%. This is substantially reduced from five years ago when the average was of the order of 18%. The main reason for this reduction is the large supply of funds and practitioners who have entered the second mortgage field. Effective rates of interest are higher for second mortgages of under $3,000 because of the constant in the expense ratio. Discounts in the Metropolitan Toronto area are now the exception rather than the rule.

A subsidiary of one of the large Acceptance Corporations has entered the second mortgage business on a formal basis. Their terms are a ten year term, a ten year amortization, 12% effective interest subject to an overall mortgage debt of not more than 80% of their idea of a fair valuation. Presently, their volume is not large, perhaps because their terms, particularly those of amortization, are not competitive. However, their entry may have the effect of stabilizing the

financing above from the lending institution base possibly 7% to 7½%. Subsequent houses or houses in non favoured areas generally carry a first mortgage interest rate of 1% above the so-called prime rate offered by the lending institutions on houses and in areas to their liking.

In the second mortgage fields effective interest rates are presently in the range of 15% to 15½. Included in such effective rate are all charges over and above usual legal fees and normal discounts. At the present time the average rate of interest for second mortgage financing in the Metropolitan Toronto area is of the order of 15½%. This is substantially reduced from five years ago when the average was of the order of 18%. The main reason for rate reduction is the large supply of funds and prospective who have entered the second mortgage field. Effective rates of interest are higher for second mortgages of under $5,000 because of the constant in the amount. Discounts in the Metropolitan Toronto area now the exception rather than the rule.

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second mortgage business in areas in which they operate. One of the larger small loan companies started a second mortgage business on a formal basis several years ago. Their volume has been small.

Although large corporations in the second mortgage market may provide stabilization, there will always be plenty of room for the non institutional practitioner. It seems that each application for financing up to the down payment has individual characteristics and special conditions. Therefore, the experienced practitioner is more likely to find a fit within the flexibility of his operations than is the institution within a firm set of ground rules.

Let us first consider a used house of a kind and in an area sought by the lending institutions in the first mortgage field. The vendor wishes to sell for one or more of a number of reasons. In the Metropolitan Toronto area a weighted distribution of reasons for sale appears to be:

1. To purchase another house - new or old 20%
2. Moving from or within the community 30%
3. Death in the family 10%
4. House too large or too small 30%
5. Straitened financial circumstances and retirement 5%
6. Divorce and separation 5%

Consider a hypothetical case. The prospective purchaser can buy a new NHA $16,000 house for $1,500 down. Let us assume that the agreed sale price for the vendor's house is also $16,000 and there is an

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5. Unsatisfactory circumstances 5%
6. Divorce and desertion 5%

Combining a owner-occupier loans. The prospective purchaser can buy a new $25,000 house for $5,000 down, but he assume that the mortgage [illegible] and there is

NHA mortgage paid down to $12,000 without any second encumbrance. The vendor who is about to buy a house in another city is looking for a $4,000 down payment and the purchaser has only $1,500 in cash. The purchaser wants to buy the vendor's house rather than a new NHA house, preferring the location and the maturity of the area. What are the alternatives available to finance this transaction?

1. Even if a lending institution were satisfied that the $16,000 sale price represents a fair valuation of the house, the maximum conventional loan at 66 2/3% in amount of $10,600 is less than the present unpaid balance of the NHA loan. Therefore, conventional refinancing through a lending institution does not help.

2. The purchaser may try to find an unsecured short term loan of $2,500 from his bank, relatives, or a finance company. Alternatively, he may seek second mortgage financing. He may well face the general rule of thumb of second mortgagees that the second mortgage is limited in amount so that the sum of the first and second mortgages does not exceed 80% of a fair valuation. In this particular example, the rule of thumb would limit the second mortgage to $800 which is too expensive a way to find such a small amount. Not only would a second mortgage of this size be unacceptable, but there would still

be a $1,700 gap.

3. The vendor may take back a second mortgage for $2,500 and then attempt to sell it in the second mortgage market. Alternatively he might pledge the $2,500 second mortgage for a loan of perhaps $1,000, which, of course, both the vendor and the purchaser would be guaranteeing. All of these exercises take time. The frustrations and delay often result in the purchaser buying a new NHA house.

I believe that over recent years the differential in down payments between new and existing houses has been an important strength in the sale of new NHA houses. It is likely that orderly and readily available financing facilities to facilitate the transfer of existing houses would have a depressive effect upon the effective demand for NHA houses.

One of the most powerful arguments which can be made for orderly and effective financing arrangements in the existing house field is that it would lead to a more efficient use of our existing stock of housing. It seems almost axiomatic that the more efficient use of any product or service will in the original instance cut down the new supply of such product or service. If at any time reliance is being placed upon new housing for employment, a case can be made against the more efficient use of existing housing at that time.

There are all kinds of permutations and

variations to the example which I have quoted. The deficiency is more acute in areas not acceptable to the lending institutions for first mortgages because all the financing must be sought from non institutional sources. In these cases the usual pattern is for the vendor to take back in the form of a first - second if there is an existing first - mortgage the balance of purchase price. If there is a first mortgage, it is likely to be a low ratio of the sale price and a substantial second mortgage is needed. Up to recently, it was usual for the vendor to sell this mortgage - usually at a discount. But more and more this type of mortgage is being pledged against a loan. The amount of loan is influenced by the 80% rule of thumb, but the rule of thumb has elasticity from 60% to 95%.

The financing of some of these transfers runs into the trouble that an existing first mortgages will not accept repayment until the end of the fifth year of the mortgage or one of its renewals. Even if the first mortgages will accept repayment, there is usually a substantial bonus payable.

Then we come to the unfinancible house adjacent to a railway track or packing plant which cannot be financed even in the second and third mortgage markets. Houses in commercial and industrial areas fall into the same category as do houses located on the main streets in the core.

This is a gap in financing sales of existing houses, not only for the reasons mentioned above, but also because of the uncertainties of being able to

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effect mortgage financing. There are ways for governmental assistance to partially meet this gap, but I doubt that there is an economic way even for Government to do so. We come right down to the basic problem of the desirability of home-ownership without sufficient financial resources. The range of this gap is so wide that there would have to be a cutoff at some point. A formal system of lending in this area might reduce the problem, but would not remove it. To the extent that Government participated, there would have to be rules and regulations of general application. The houses, areas and financial circumstances vary so greatly in every case that rules of general application would be difficult to draw and almost impossible to implement. The administrative costs would be very high and it is difficult to visualize the source of experienced staff. All in all, I believe that steps to close this gap would be too costly both in administration and loss ratio and could not be administered in a fashion that would be publicly acceptable in equality of treatment.

Suggestions have been made that the statutory limit of loan ratio for loan, life and trust companies be increased from 66 2/3% to 80% in an effort to close part of this gap. A strong case can be made against such a change unless Government guaranteed the 13 1/3% differential. One of the objections to such a step is that the relief would fall only in those areas acceptable to the lending institutions whereas the gap is in its most acute form in other areas.

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into existing house field which in number of sales appears two to three times the size of the new house field. This would be almost the equivalent of a system of insuring the financing of amounts above existing mortgages with the additional burden upon available funds of refinancing the existing encumbrances of first mortgage dimension. As in the United States it would fill the need in the newer areas where the principles of mortgage selection could be made applicable. The ratio of loan to value would determine the amount of coverage. Maintenance of mortgage insurance principles would, as in the United States, limit its application in older areas where financing a sale is most difficult.

As an argument against extending NHA financing to existing property, there is concern about the monetizing of existing savings. The argument is that if NHA loans on existing houses are not limited to funds required to finance the purchase price, house owners would borrow for other purposes. The net effect would be a higher mortgage debt ratio. This argument is hard to follow because if a home owner has savings in the form of equity in his house, he would seem to be just as entitled to pledge such equity as he is to pledge Canada bonds to produce funds for such purpose as seems desirable to him.

In the United States where existing houses have been financed under the FHA since the mid 1930's, no great harm seems to have been done. The same argument would cast doubt upon the propriety of an owner of an unencumbered house taking a 50% conventional loan

because it was not good for him. I doubt the suitability of this paternalistic approach. Twelve years ago, anything above a 50% conventional loan was the exception. Today, lending institutions are making conventional loans to a very full 66 2/3%. This monetization of existing savings does not seem to have been too damaging.

FLOW OF MORTGAGE FUNDS

Looking at capital markets in the Post War years, there would seem to be little argument but that the housing sector has been the weakest borrower and for that reason has had the most support by Government. In my view, mortgages for housing of all kinds are more difficult to obtain than even mortgages on commercial property. The inflexibility of a mortgage as such and the requirement that the selection of a mortgage portfolio is the selection of a great number of separate and distinct transactions with varying risk has had the effect of making mortgages one of the less desirable forms of investment. In addition, there is the non liquidity feature.

In the years 1949, 1953 and 1959 steps were taken to increase the flow of mortgage funds into the housing sector because an optimum volume of new starts was limited by the lack of funds. Steps will have to be taken before long to cure the present hiatus. Although it is too early to say that housing starts are now limited by the lack of NHA funds, it is likely that before too long steps over and above direct lending by

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This intermittency in the flow of funds has in itself been the main sluggishness of the post war mortgage market. Although there is plenty of room for improvement there seems nothing basically wrong with the Canadian mortgage structure save for some of the gaps recited earlier and the too regular interruptions of the flow of NHA funds.

The mortgage structure works very well provided that it is fed with sufficient funds. Perhaps one of its structural weaknesses is the small proportion of local institutions. In the United States, particularly in the mortgage origination field, there is a domination by local institutions familiar with local conditions and local borrowers. In the Province of Quebec, we do have a healthy proportion of local institutions. However, for Canada as a whole the mortgage scene is dominated by national institutions.

An improvement in the Canadian mortgage structure can best be effected by closing some of the gaps and improving the flow of mortgage funds. Indeed, an improved flow will indirectly help to close some of the gaps. The balance of this memorandum will be devoted to reference to possibilities of a more ample flow of mortgage funds. The optimum in mortgage financing for the housing industry would be a condition in which new housing starts were limited by effective demand only.

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about there being too much mortgage money available resulting in over building. The usual example cited is 1958. I have doubts that this is an important problem because any overbuilding in that or other years is quickly corrected by the lack of effective demand. I see nothing particularly wrong with an inventory of houses and rental units. If there is merit in the filter or hand-me-down system then benefits will only flow to those who cannot afford new housing if there is a reasonable inventory of new housing. Presently, there is a very full inventory of rental housing in our larger cities. Although one hears comment about completed but unsold houses as if there was something reprehensible about a long housing position, the situation today is that the inventory of new completed but unsold housing is about two and a half weeks production. If the filter process is to really work, there must be a larger inventory of new houses. The mortgage investor does not like an overbuilt condition or declining prices because the stability of a mortgage portfolio flourishes in an economy of scarcity.

Other than in the four periods of restraint in the flow of mortgage funds mentioned earlier in this memorandum, there is little evidence that new residential construction of NHA standard has been limited by the lack of mortgage money. Elimination of intermittent periods of restraint seem more important than substantial changes in our mortgage structure. In my view, additional sources of mortgage funds are required for three purposes:

about there being too much mortgage money available resulting in over borrowing. The usual economic cliche I hope. I have doubts about that is an important problem because our overburdening in that on other years is quickly corrected by the lack of effective demand. I see resulting particularly wrong with an inventory of houses and rental units. If there is merit in the filter or trading-down system then benefits will only flow to those who remain. Afford new housing if there is a reasonable inventory of new housing. Presently, there is a very full inventory of rental housing in our larger cities. Although one hears comment about completion out there it seems as if there was something reprehensible about a long bonding position, the situation today is that the inventory of new completed housing is about two and a half weeks production. If the filter process is to really work, there must be a larger inventory of new houses. The mortgage investor does not like an overbuilt condition or declining prices because the elasticity of a mortgage portfolio flourishes in an economy of security.

Other than in the four periods of readjustment in the flow of mortgage funds mentioned earlier in this memorandum, there is little evidence that non residential construction of FHA standard has been limited by the lack of mortgage money. Substitution of investment positions of resultant been more important than substantial increase in our building economy. In my view, conventional sources of mortgage funds are adequate

(a) To ease periods of restraint.

(b) A larger supply and more regular availability of mortgage funds will have the effect of reducing and easing some of the gaps.

(c) Availability of more mortgage funds will have the effect of reducing the cost of mortgage money.

The case has been made that the capital pie is only so large and if more resources are diverted into the housing sector, there will be insufficient left for equally important activities. The answer to this is that there is no more important activity than increasing our housing stock. It could also be argued that other sectors of demand for capital funds have had an easier time in finding funds than is justified by their relative position in the scheme of things. The pie cannot be divided in mathematical exactitude. The best that can be done is to remove some of the difficulties and increase the availability of mortgage funds so that the housing sector may be in a more fair and better competitive position. Higher interest rates is an obvious way of achieving this end. But equally effective, though more difficult, would be to remove some of the disabilities from mortgages as an investment instrument, so that present and potential capital markets would be more receptive to mortgages as an investment.

The hiatus in the flow of mortgage funds which has occurred on a number of occasions in the Post War period has been caused by different reasons. In

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1949 the basic trouble was that the institutional lenders had little faith in effective demand both in the rental and home ownership fields. The steps which successfully met this hiatus was the introduction of an extra one sixth loan financed by Central Mortgage to reduce equity requirements and the introduction of rental insurance. These steps were reasonably effective. When it came time to turn down the volume of new housing on account of the Korean crisis, the removal of the extra one-sixth and the cessation of rental insurance were equally effective.

In 1953 it became obvious that the pools of savings constituting the institutional investors were insufficient to finance the required amounts of housing. Agency loans were introduced whereby the lending institutions advanced CMHC funds on an agency basis with an option to buy the loans. All options were subsequently exercised. This was the first major injection of CMHC funds into the mortgage market. Direct lending was not involved. Agency loans were but a stop gap. To meet the real need the chartered banks were introduced into the mortgage business in 1954. Their enthusiasm for NHA loans provided an effective solution to the problem then existing.

The hiatus which occurred in the Fall of 1959 was occasioned by monetary conditions. Then as today the differential between the maximum NHA interest rate and other forms of investment became too narrow. Mortgage lending under the NHA ceased and conventional mortgages became available only at high interest rates.

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In December, 1959, NHA downpayments and amortization were eased and the maximum rate of interest was moved from 6% to 6 3/4%. In the first half of 1960 yields on Canada bonds reduced to a point that the new NHA interest rate became attractive. These steps accomplished their purpose.

The present position is not unlike the hiatus of the Fall of 1959 in that the present 6½% NHA rate is unattractive.

In the United States, although there are intermittent periods of ease and restraint, they do not seem to experience the same periods of absolute cessation. There is good reason for this difference. Their system of discount allows market forces to operate so that at some price FHA loans continue to be made. I hold no brief for the introduction of the discount system in the NHA. But I do think that some flexibility could be found without completely abandoning the principle of a par transaction between lender and borrower. A fluctuating interest rate authorized by Government may prove more embarrassing than the discount system under which the uncomfortableness of a variation in authorized interest rate is well hidden. But it makes more sense. What is important is that some technique be found to bring an end to the periods of hiatus such as the one now being experienced.

Maximum interest rates under the NHA have developed an importance beyond the NHA itself. There is evidence which suggests that the maximum NHA interest rate is a yardstick or bench-mark for mortgage interest

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rates in the residential and commercial conventional fields. For instance, conventional loans on individual houses have for a number of years carried an interest rate in the range of one-quarter to one-half of one per cent in excess of the maximum NHA interest rate. This rate has been very responsive to changes in the NHA rate. The same differential has been present in the conventional apartment house field. Commercial mortgage loans have a wider variation in interest rate but there is some correlation to the NHA interest rate.

Although material is being prepared to show the correlation between the level of interest rates and the volume of new housing starts, I anticipate these findings with the view that effective demand for home ownership by those who can afford it is relatively impervious to the absolute level of interest rates. The real effect of higher interest rates is upon the effective demand for housing by narrowing of the band of families who can qualify under the limitation that the mortgage debt service does not exceed 27% of their income. Assume that in Metropolitan Toronto the minimum income to qualify for a minimum house with a $14,000 mortgage at 6½% is $5,200. If the interest rate were 5% the mortgage debt service would be reduced by $126.00. On the basis of the 27% limitation income requirements would be lowered to $4,733. The widening of the band of eligible purchasers would increase effective demand. In my view the major implication of interest rates is upon effective demand rather than upon the attitude of the home owner to

6½% interest rate as such. I am afraid that NHA interest rates at any level have a higher degree of acceptability because they are established by government rather than by a lender.

On the other hand, there may come a level at which interest rates become unacceptable per se. In the Metropolitan Toronto area real estate firms report that some re-sales become difficult if the existing mortgage loan is more than 7% - a kind of barrier like the four minute mile. There are cases where this revulsion against interest in excess of 7% is so great that one of the conditions of sale is that the vendor shall prepay all interest due to the mortgagee in excess of 7%. It is interesting to note that this is in a climate of a maximum NHA rate of interest of 6½% which is too low to be operative. I mention this present 7% barrier as a matter of interest rather than of importance. It does not change my views upon the effect of the NHA interest rate nor that the conventional interest rate will continue its historical spread of ¼% to ½% above the NHA rate.

Apart from the gaps mentioned earlier in this memorandum, it would appear with CMHC participation that we had sufficient funds to finance not only the current rate of new residential construction, but also a substantial volume of re-sales. But even so, it is probably desirable to find additional sources of mortgage money not only to improve the terms upon which it can be borrowed and to provide a cushion for periods of restraint in mortgage lending but also to relieve Central

Mortgage of the necessity to supply such a large proportion of the funds. I have mentioned earlier that this activity by Central Mortgage has had the desirable effect of closing practically all the gaps in financing new housing where NHA standards and borrower requirements are met. Funds for the closing of these gaps is but a small fraction of the flow of mortgage funds from Central Mortgage. The major direct lending activity is in the areas of sluggishness. Under our system there is much to be said for a maximization of mortgage funds from the private sector, even if it is the subsequent policy of Central Mortgage to sell their portfolio to private investors. Residual lending by Central Mortgage might well be limited to the filling of gaps of private lending - NHA or conventional. Practically this can only be accomplished by the introduction of other sources of mortgage money or increase from present sources. Even if there were no problem in Government supplying the funds for direct lending by Central Mortgage, there are potential dangers to the mortgage market as a whole in a large proportion of mortgages having privity of contract between an agency of government and the borrower. Moreover, if like sums of public funds are readily available to Central Mortgage, there is plenty of room for their investment in a more vigorous public housing program, -- the greatest gap of all and one which cannot be filled by any form of private lending.

SOURCES OF MORE MORTGAGE FUNDS

Let us assume that for these or other reasons it is desirable to have a wider and larger source of mortgage funds. There is the consideration of where these funds shall be found and the terms and technique for such additional mortgage investment to take place. Among the possibilities are:

1. The return of the chartered banks to the NHA mortgage field would be the most important help. The arguments for their participation are as strong today as they were in 1953. It may be that the future volume of lending by the banks will not be as large as it was in the four years 1955 to 1958, when it averaged 239 millions a year. A continuing mortgage investment program of even half of this amount would be helpful. Not only would it supplement mortgage lending in those areas presently covered by the lending institutions, but it would also have the effect of assisting Central Mortgage in filling some of the gaps in the outlying areas. The very large branch office system of the chartered banks is a most important instrument for full national coverage in mortgage lending. Although steps must be taken one at a time, I look forward to the day when the chartered banks may also be in the conventional field.

2. From time to time there has been discussion about the availability of non resident mortgage funds from abroad usually from the United States. The reported amount of the potential transactions is usually in multiples of $100 Million, although

occasionally fractional amounts of $50 Million are reported.

There is difficulty in locating more than two specific instances of mortgages having been purchased by non residents. One was a direct investment in NHA loans in amount of about $1,250,000. The other involved the purchase of some $5 Million of debentures secured on a 125% basis by NHA loans held by a trustee for the debenture holders.

There have been a number of non resident portfolio investors examine the possibilities of investment in NHA loans because they were attracted by interest rate and by a guarantee more favourable than the FHA guarantee. There are three conditions which have restrained non resident investment in NHA mortgages, and I believe that they are equally applicable to conventional mortgage investments.

(a) With very few exceptions, Canadian mortgages are written in Canadian dollars. The non resident cannot find a practical long term exchange hedge.

(b) Although mortgage interest rates in Canada are traditionally higher than those in the United States, the withholding tax is not pleasing to the non resident investor. This difficulty is very real for U.S. pension funds because the withholding tax is a net deduction from investment income without any corresponding credit against U.S. taxes.

(c) Non resident investors who do not carry on

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business in Canada have fears that making or even owning mortgages in Canada will be deemed to be doing business in Canada. Whether such is the case has never been resolved, but the uncertainty has been a deterrent to non resident investment to the Canadian mortgage field.

Because there do not appear to be easy answers to these difficulties, there seems little immediate likelihood that the supply of mortgage funds will be supplemented by investment from abroad.

3. The recent change in the Trustee Act of Ontario and of some other provinces, making NHA mortgages eligible as trustee investments, has the possibility of opening up another source of mortgage funds. In larger estates where re-employment of funds arising from monthly amortization payments is not a problem, and where distribution is not to be made for many years, NHA mortgages may prove to be an acceptable type of investment. Where distribution is anticipated within, say 15 years, the question arises as to liquidity. A secondary mortgage market, clearly identifiable as such, might make NHA mortgages more attractive to executors of estates. NHA mortgages as against conventional mortgages should be attractive to estates because of the guarantee, the relief from funds being required to protect defaults and relief from the ownership of foreclosed real estate.

4. Pension funds would appear to be one of the largest potential sources of mortgage funds. Such a

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large and rapidly growing pool of savings so unimportant as a source of mortgage money is something of a phenomenon. Not only is their present asset size impressive at some $4\frac{1}{2}$ Billion, but their current annual rate of increase of these assets at $12\frac{1}{2}\%$ indicates their importance in the future. Their assets have a low mortgage ratio of about 5% as against about 38% for the life insurance companies. If a 38% mortgage ratio is appropriate for life insurance companies, then a case could be made that at least as large a mortgage ratio would be appropriate for pension funds whose liabilities are generally even more long term than are the liabilities of the life companies.

Under present arrangements pension funds, trusteed or self-administered, can find economic ways to hold a mortgage portfolio without establishing their own mortgage departments. The guarantees under the National Housing Act protect the pension funds not only against the continued ownership of foreclosed real estate, but also against the necessity of investing funds in borrowers charges to protect delinquent mortgage accounts. The extra interest earnings above Canada bonds should have attraction to pension funds whose liabilities are not as fixed as those of the life companies. Over the years there is a tendency for an increase in the liabilities of a pension fund by reason of increases in benefits and an upward movement in salary level.

Already some pension funds have been able to buy NHA loans in blocks. A secondary mortgage market

would provide pension funds with an orderly way to make investments in mortgages in amounts to match their investible funds.

5. From time to time there has been comment about the feasibility and desirability of a secondary mortgage market. It has been suggested that some steps towards this end have already been taken.

The shape and form of a secondary mortgage market is a matter of judgment and opinion. However, its objectives carry a reasonable degree of unanimity. For the purposes of this memorandum, it is assumed that the aims and objects of a secondary market are:

(a) To reduce the fluctuations in the flow of mortgage funds which would contribute to efficiency in housing construction.

(b) To introduce liquidity and marketability of mortgages to the end that mortgages would become a more attractive investment, not only to portfolio investors, but also to private individuals and estates.

(c) To reduce the cost of borrowing on the security of residential property so that the borrower would benefit from reduced costs on doing business on the part of the primary lender. The borrower would gain from assured marketability which might increase the volume of funds seeking mortgage investment.

(d) To remove present general inhibitions surrounding the movement of funds between mortgagees.

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(e) To remove the historical tendency of many portfolio investors to regard mortgages as a residual outlet for funds.

(f) To create a greater responsiveness of mortgage investments to changes in interest rates.

(g) To improve mortgage market conditions to reduce the competitive shortcomings of mortgages as an investment instrument.

There are certain practices in Canada which are elements of a secondary mortgage market. Among them are:

(a) Conventional mortgages - although in relatively small amounts - have been bought and sold for years.

(b) The sale of guaranteed investment certificates or their equivalent secured by first mortgages and sold to individuals is an important element of a secondary mortgage market. The debenturization of mortgages is a Canadian custom now being sought by the proponents of a secondary mortgage market in the United States.

(c) Even in the Joint Loan days of the NHA a few transfers did take place between institutional approved lenders.

(d) The National Housing Act of 1954 establishes an approved method whereby insured mortgages can be transferred provided their administration continues to be handled by an approved lender.

(e) The Central Mortgage and Housing Act provides

(e) To remove the historical tendency of many portfolio investors to regard mortgages as a residual outlet for funds.

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(d) The National Housing Act of 1954 established an approved method whereby insured mortgages can be transferred provided their administration continues to be handled by an approved lend-

statutory powers more than sufficient to allow that institution to act as a central mortgage bank to which access could be given to private mortgage banks operating in the secondary market.

(f) Since the introduction of the insured mortgage technique the trust companies have been originating NHA loans for sale to portfolio investors, chiefly pension funds. This may not be considered a secondary mortgage transaction, any more than the originating activities of a branch office or a correspondent of a lending institution, in that during the period of holding generally the originator is not on the risk of a change in value of the mortgage. In most cases there has been a prior commitment by a pension fund to "take out". Therefore, the function may be considered to be that of an agent, rather than an operator in a secondary mortgage market.

(g) The four auctions of NHA loans originated by Central Mortgage has started a larger flow of transfers. For the most part these transactions have been a direct transfer from a Government portfolio to an institutional portfolio. In lesser amount investment entrepreneurs have been the purchasers with pre-arranged subsequent sale to institutional portfolios. In still lesser amount there have been transactions in which the investment

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entrepreneur has taken a position without prior commitment of "take out". This has been a secondary mortgage market operation in the fullest sense.

These are the early steps, and although not an impressive list, should not be minimized. If a secondary mortgage market is to be developed, then it is well that these precedents are behind us rather than before us.

Before attempting to suggest what might well be the elements of a secondary mortgage market in Canada it may be helpful to make references to like circumstances in the United States.

(a) The development of a real secondary mortgage market is under active consideration and the need for such facilities seems to have general recognition and acceptance.

(b) The operations of the Federal National Mortgage Association and the Federal Home Loan Bank system, although helpful, do not fulfill secondary mortgage market functions.

(c) There seems general agreement that a satisfactory secondary mortgage market cannot be successfully developed without private mortgage banks willing to stand in the market place on both the buy and sell sides on their own account and at their own risk.

(d) There seems to be unanimity in the view that private mortgage banks in the secondary mortgage market can be more effective if

assisted by the facilities of a central mortgage bank.

(e) There is a very elaborate system of mortgage correspondents in the United States who style themselves as mortgage bankers but essentially are mortgage agents operating under credits from commercial banks with pre-committed "take outs" from portfolio investors. On occasion these correspondents do get into a "long" position but it is estimated that about 99% of the mortgages processed by correspondents and mortgage bankers are with the benefit of a pre-committed take out. In the United States it is not customary for institutional holders of mortgage loans to make progress advances. Their system is for the institution to acquire completed mortgages thus leaving with the correspondent or mortgage banker the function of arranging and finding both long term and construction financing for the merchant house builder.

(f) Consideration of this problem in the United States leads to the belief that a secondary mortgage operation can be more easily applied to FHA loans because of their greater uniformity and because of the guarantee feature. More difficult would be a secondary market operating in conventional mortgages. But the consensus seems to be that the secondary mortgage operation should embrace

assisted by the facilities of a central
mortgage bank.

(e) There is a very significant aspect of mortgage correspondents in the United States who are themselves as mortgage bankers but essentially are mortgage agents operating under credits from commercial banks and pre-committed "take outs" from permanent investors. On examination these correspondents do get into a "long" position but it is estimated that about 90% of the mortgages processed by correspondents and mortgage bankers are with the benefit of a pre-committed take out. In the United States it is not customary for institutional holders of mortgage loans to make progress advances. Their system is for the institution to acquire completed mortgages thus dealing with the correspondent or mortgage banker the function of arranging financing for the developer-builder.

(f) Consideration of this problem in the United States leads to the belief that a secondary mortgage operation can be more easily applied to Fair Lease because of their greater uniformity and because of the guarantee feature. Note difficult would be a second market operation to conventional mortgages but the experience seems to be that the

both classes of mortgages.

If it were considered desirable to have a secondary mortgage market in Canada attention might be directed to these considerations:

(a) In the original instance emphasis might well be placed upon NHA loans because the inclusion of conventional loans presents even greater difficulty in Canada than in the United States due to the lack of a title guarantee system.

(b) Encouragement to the establishment of private mortgage banks to deal in the secondary market might be given by facilitating charters under the Loan Companies Act which would appear to be the most convenient form under which mortgage banks could operate in the secondary mortgage market. They need not be called banks.

(c) Although not necessary, a helpful contribution to better market conditions would be for the powers already vested in Central Mortgage to be used as a central mortgage bank to which practitioners in the secondary mortgage market would have access. Conditions of such access would be predetermined in the form of ground rules. The powers of a lender of last resort should have different application to practitioners in the secondary mortgage market than to portfolio investors. A similar differential exists in the Canada bond

both classes of mortgages.

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to prescribed classes in the secondary mortgage

market then to provide liquidity. A simi

field. The lines of demarcation are not quite as clear in the mortgage field but differentiation could be established.

(d) Practitioners would be encouraged to enter the field and their business would be carried on more effectively if with suitable correlation.

(i) the chartered banks, so enabled by legislation, would take a forward look at the provision of short term warehousing funds, and

(ii) a central mortgage bank or Central Mortgage under its present powers would make credits available as a lender of last resort.

(e) Greater flexibility in the NHA interest rate to more closely reflect market conditions is required. For the secondary mortgage market to be effective, there should be a market in mortgages as they are being originated. Unless there is a flexibility of interest rate, there will be a tendency for the secondary mortgage operations in the originating field to take place only when there is a comfortable spread in interest rates between mortgages and bonds. In conditions like the present an insufficient NHA rate makes unmarketable what mortgages are now being originated.

(f) The classification of mortgages will be an

(d) Homeowners would be encouraged to enter
the field and their business would be carried
on more effectively if with suitable safe-
guards

(i) the clearer and more readily enforced by
Registration would make a foreman loan
as the purchaser of every new mort-
gage funds; and

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(e) Greater flexibility in the NHA insurance may
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being in demand

essential element of a secondary market. The originator, the market maker and the portfolio lender must know what they are selling and buying. Included in such classification is the age of the mortgage, equity, payment record, location, and present condition of the property. In the four auctions by Central Mortgage, there has been a substantial spread in the bid prices on account of classification factors.

(g) One of the main reasons for a central mortgage bank is to make available to the market prompt and complete knowledge of the going prices for mortgages. The market should have knowledge of the day-to-day transactions as well as bid and offering prices. Current information about the mortgage market, primary and secondary, should be made available.